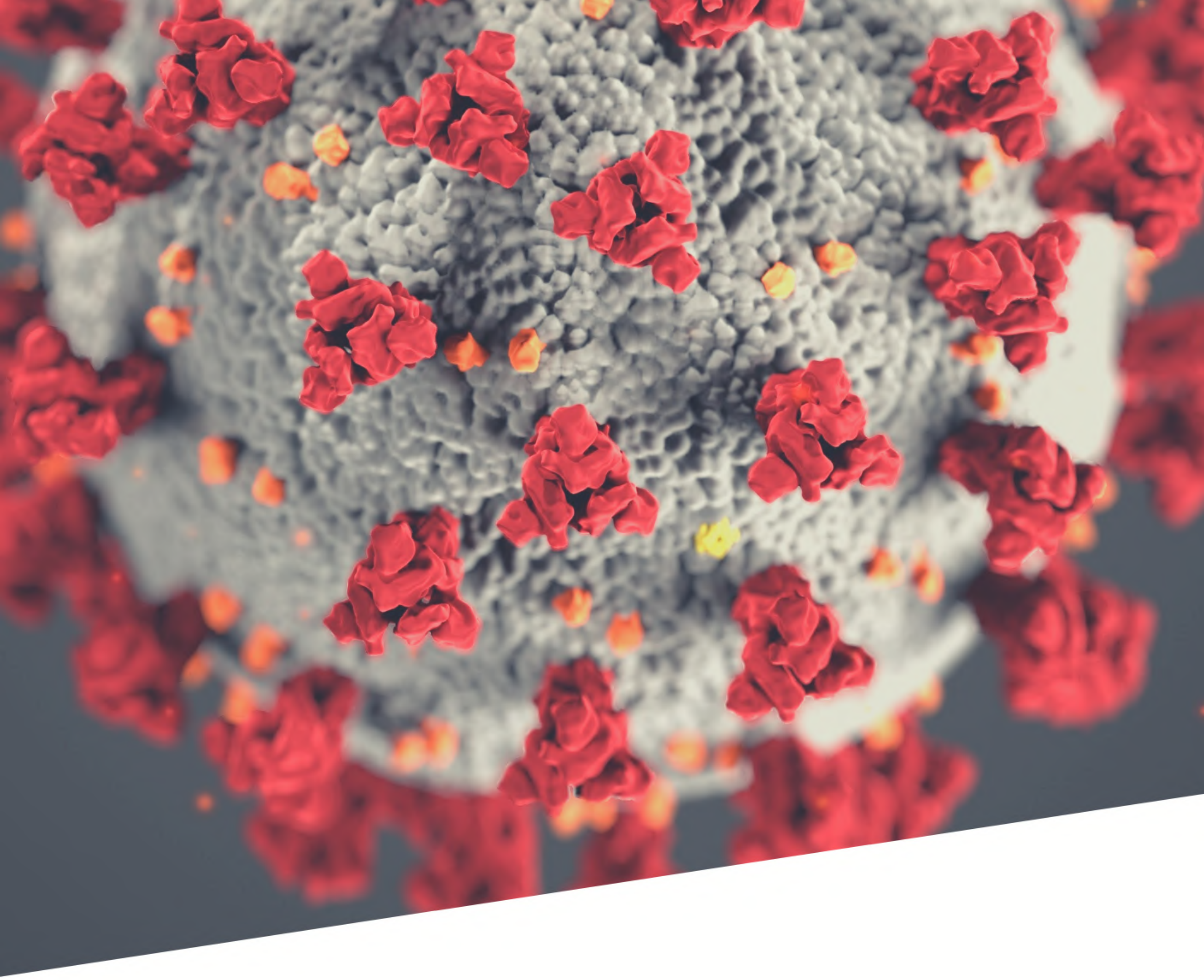

A ROAD MAP FOR ECONOMIC RECOVERY

EUROPE AFTER THE CORONAVIRUS

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Executive Summary

The economic shutdown caused by the current pandemic is putting pressure on policymakers to design programs to support businesses and workers. It is currently unclear how long the health crisis will last or what the economies of Europe will look like in the aftermath. Governments should be ready with appropriate policies to answer the circumstances as they shift.

This is clearly a health crisis, first and foremost, and policies should be designed with that in mind. However, the economic effects of the health crisis are substantial and fiscal and monetary programs deployed in response to the crisis need to be well-targeted and designed. Once the health crisis abates, there will be challenges for policymakers in evaluating ways to address new debt burdens, the speed of the post-crisis recovery, and the risks of another wave of infections.

European institutions and individual countries should work together to avoid allowing the economic shutdown to turn into a prolonged depression. The business closures and social distancing policies come with costs even if those costs are difficult to compare to a scenario in which the pandemic was allowed to spread further.

This paper evaluates how governments in Europe should be designing economic policies to minimize the economic shock while the health crisis continues, and then shift to policies that will help economies recover and return to a sustainable fiscal footing in the context of growth.

Weathering the Storm

The current economic shutdown calls for significant economic relief. The income that businesses and workers are currently missing will need to be replaced, temporarily, by government support. These policies should not be aimed to stimulate economic activity because that is generally at odds with the health goals of the economic shutdown. These policies should be explicitly designed to be temporary and should be conducive to long-term growth.

- Individual countries should continue to provide:
    - Delays or deferrals of significant tax payments by businesses and individuals.
    - Targeted tax credits and tax reductions, including accelerated capital allowances for businesses.
    - Direct fiscal support to businesses and workers, including those with reduced hours, to address the costs of the economic shutdown.
- European institutions should focus efforts on:
    - Supporting necessary cross-border trade and travel, such as by deferring or suspending duties and VAT.
    - Providing flexible, temporary financial support to countries that require resources.

Harnessing the Recovery for Long-term Growth

Once the health crisis is abated and the economy begins to recover, governments will need to support the recovery with policies that promote sustainable growth. Targeted stimulus measures or near-term austerity programs could undermine prospects for a broad recovery. Businesses will need support through well-designed income taxes, and governments should focus revenue-raising efforts on broad-based consumption taxes.

- Individual countries should:
  - Focus on pro-growth income tax policies that support business investment and hiring by reducing the cost of capital through expanded capital cost allowances and lowering the tax burden on labor.
  - Rely on broad-based consumption taxes as mechanisms to support fiscal sustainability.
- European institutions will need to:
  - Provide an adjustment period before enforcing fiscal rules until an appropriate growth threshold has been met.
  - Support member countries' pro-growth tax and spending policies by avoiding adoption of contrary policies at the EU level such as distortionary digital taxes and financial transaction taxes.
  - Ensure countries are not limited in adopting the tax policies they think are most beneficial in the current situation by avoiding centralizing tax policy decisions.

Introduction

The coronavirus has led us into one of the biggest crises in decades, possibly even the largest since World War II. The virus, having originated in Wuhan, China, has swept over the entire European continent. As of early April, more than 1.9 million people worldwide have been infected by COVID-19 (the actual number probably being much higher[1]), with more than 120,000 dying from it.[2] The virus has brought several countries, in particular Italy and Spain, to their knees. And lockdown measures have halted public life throughout Europe.

Similarly, the economy has been in free fall since lockdown measures were implemented. The virus has put a major strain on economic actors, particularly small and medium-size businesses, workers, and the poor. For all intents and purposes, the European economy is on pause at the moment, with only a narrow list of "essential activities" still operating. Due to lockdown measures, the economy is faced with a radical supply shock, which cannot be solved by traditional economic, fiscal, and monetary policies.

This is particularly worrisome considering economic growth was already slowing in recent months, with some countries barely reaching positive growth territory in 2019.[3] Meanwhile, a lack of fiscal health in many European public finances has—at least theoretically—limited policy options to keep the economy going during the crisis. A major debt crisis could subsequently be the logical consequence with countries like Greece (178 percent debt to GDP), Italy (137 percent), Portugal (120 percent), Belgium (102 percent), and France (100 percent) already deeply indebted.[4]

As a response to the crisis, European governments, in cooperation with EU institutions, have passed programs and support schemes of over €2.77 trillion,[5] the European Central Bank also having become increasingly active.

With the economy on break and (tens or even hundreds of) millions of people in danger of financial ruin, there is no doubt that significant support needs to be provided during this crisis. Economic relief could effectively help those most affected financially by COVID-19 until the spread of the virus has been contained.

[1] Nina Schwalbe, "We could be vastly overestimating the death rate for COVID-19. Here's why," World Economic Forum, Apr. 4, 2020, https://www.weforum.org/agenda/2020/04/we-could-be-vastly-overestimating-the-death-rate-for-covid-19-heres-why/.
[2] As of April 14. Johns Hopkins University & Medicine Coronavirus Resource Center, "Coronavirus COVID-19 Global Cases," https://coronavirus.jhu.edu/map.html.
[3] Eurostat, "Real GDP growth rate – volume," Apr. 8, 2020, https://ec.europa.eu/eurostat/databrowser/view/tec00115/.
[4] Eurostat, "General government gross debt - quarterly data," Jan. 31, 2020, https://ec.europa.eu/eurostat/databrowser/view/teina230/.
[5] The numbers are from April 7, 2020. European Commission, "Economy," https://ec.europa.eu/info/live-work-travel-eu/health/coronavirus-response/economy_en.

However, the toolbox of different short-term policies is large, with both good and bad policies taken into consideration. It is important that national governments as well as the EU are following a prudent path, which is not simply oriented to “doing something,” but to actually do good.

Furthermore, governments need to plan ahead for a post-coronavirus world when restrictions will be lifted. A fast yet sustainable economic recovery will be needed. Thus, it is essential to think of possible long-term reforms and how to pivot from short-term, temporary mechanisms to long-term policies that can promote growth.

In the following, we will examine different proposals and already implemented programs for both the short as well as long run, which can fulfill the purpose of offering support and relief now and would enable an economic spurt upon a return to normalcy.

Immediate Policy Response

The challenge of the current outbreak requires a strong short-term response to protect public health and to bridge the economic gap between shutting down a significant share of economic activity and then reopening the economy. While European countries are providing different fiscal relief measures, there are some key themes in the responses:

1. Delaying or deferring significant tax payments
2. Targeted tax reductions
3. Broad fiscal relief

In some countries, the response to the crisis shows weaknesses in current tax policies. Good tax policy should be designed to raise sufficient revenue without creating unnecessary economic harm. Unfortunately, the policies baked into some country’s tax systems are requiring governments to make significant changes in a short time period to minimize the impact of the economic shutdown.

Policymakers should be cautious, however, in framing the response to the crisis. The fiscal relief packages should be designed to be a bridge through this difficult time. The near cessation of economic activity does not lend itself to stimulus policy. In fact, stimulating more economic activity is contrary to the goals of the economic shutdown. Relief is certainly in order, but policymakers should be considering short-term policies that will also be conducive to longer-term prosperity after the crisis abates.

Examples for the way these policies work in different countries and potential EU-level policies can help governments across Europe identify the best policy mix for the short term and avoid mistakes that could harm the longer-term recovery.

Germany Has Moved Kurzarbeit Into High Gear

One response that has been modeled in different ways across Europe is the subsidization of reduced work hours. In Germany, this *Kurzarbeit* (short-term work) policy has been expanded.[6] The current policy provides that:

- Retroactive to March 1, 2020, businesses can register for the scheme if 10 percent (previously 30 percent) of their employees face income reductions of more than 10 percent due to the current crisis.
- The subsidy amounts to 60 percent of lost after-tax wages (67 percent if the employee has at least one child).
- Social security contributions paid on the reduced working hours will be refunded.
- The wage subsidy can be collected for up to 12 months.
- Temporary workers are also eligible.

The German government estimates that 2.35 million employees—about 5.5 percent of the total workforce—will receive benefits from this policy during this current crisis.[7] At the height of the financial crisis of a decade ago, 1.4 million workers relied on this program. The additional costs are estimated at €10 billion, including €6 billion in social security contribution refunds and €4 billion in short-term work money.[8] More recent numbers suggest that those estimates will be far below the actual use and cost of this program.[9] The Federal Labor Office—financed through worker and employer contributions—has built up reserves of €26 billion that can be drawn upon.

The policy fits the current crisis well because it both allows businesses to keep their current employees and provides a benefit to workers who are seeing reduced hours due to the economic shutdown. The wage replacement level is also not too high to freeze the labor market at a time when some sectors (healthcare, logistics, and grocery stores) are hiring workers for what may be temporary roles.

Norway (Temporarily) Adjusts Tax System Weaknesses

The fiscal response in Norway has highlighted some of the weaknesses of the country's tax system. Norway is providing support with a new loss carryback provision, wealth tax relief, targeted VAT relief, and various tax payment delays.

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[6] Bundesfinanzministerium, "Corona-Schutzchild: Kurzarbeitgeld," Mar. 19, 2020, https://www.bundesfinanzministerium.de/Content/DE/Standardartikel/Themen/Schlaglichter/Corona-Schutzschild/2020-03-19-Beschaeftigung-fuer-alle.html.

[7] Guy Chazan and Richard Milne, "Kurzarbeit: a German Export Most of Europe wants to buy," *Financial Times,* Mar. 23, 2020, https://www.ft.com/content/927794b2-6b70-11ea-89df-41bea055720b.

[8] Henrike Roßbach, "So viele Kurzarbeiter wie noch nie," *Süddeutsche Zeitung*, Mar, 19, 2020, https://www.sueddeutsche.de/politik/kurzarbeit-corona-bundesregierung-1.4851667.

[9] Carolynn Look, "Explaining Kurzarbeit, Or Saving Jobs the German Way," Bloomberg.com, Apr. 3, 2020, https://www.bloomberg.com/news/articles/2020-04-03/how-germany-pays-workers-when-their-work-dries-up-quicktake.

Loss provisions are important features of any tax code and can help businesses weather hard times more easily.[10] Norway does not generally provide loss carrybacks, however, and the government needed to act to be able to allow businesses to reduce previous tax payments using current losses.

Wealth taxes are also not designed to take economic downturns into account. A family business owner subject to a wealth tax may need to take cash out of their business to pay the wealth tax. In times of economic hardship, that need for shifting money from the business to the owner may put the business at risk of solvency.

Norway's wealth tax of 0.85 percent (on net wealth above NOK 1.5 million, or €134,000) could have caused such problems in the wake of the economic shutdown. To address those issues, the government is temporarily postponing payments of the wealth tax for individuals whose net wealth includes businesses that are running losses. These changes temporarily relieve the pressure of the tax and allow companies to keep more cash in their businesses.

Both of these changes show how policy responses to the crisis can conform to longer-term policy objectives that support growth and investment. Instead of measures to provide temporary relief, Norway could make loss carrybacks a permanent feature of the corporate tax system and use the temporary delay in the wealth tax as an opportunity to permanently shift from that form of taxation.

Italy Allows Banks to Deduct the Future, Now

In the countries hardest hit by the pandemic, the economic crisis will likely be the worst. Italy has moved to provide fiscal support in a variety of ways, but one particular measure shows how countries can trade future tax deductions for current tax relief.

The general economic shutdown and debt moratorium are creating serious challenges for Italian banks. To alleviate some of the pressure on the banking system, the government is allowing banks to convert losses on some of their loans into tax credits.[11]

This targeted relief could be used as a template by other countries. Businesses of all types take deductions on previous losses or on depreciation allowances. Governments could provide extra tax relief by allowing businesses to convert those future deductions into current tax relief. Essentially, instead of continuing to deduct losses over the next several years, a business could opt to take those losses now in the form of a refundable tax credit of equivalent value. For the

[10] Michael P. Devereux and Clemens Fuest, "Is the Corporation Tax an Effective Automatic Stabilizer?" *National Tax Journal,* 62:3 (September 2009), https://www.ntanet.org/NTJ/62/3/ntj-v62n03p429-37-corporation-tax-effective-automatic.pdf.

[11] EY, "Italian NPLs, and UTPs: conversion into tax credits of Deferred Tax Assets associated with tax losses carried forward and other deferred deductions," Tax News Update, Global Edition, Mar. 18, 2020, https://globaltaxnews.ey.com/news/2020-5396-italian-npls-and-utps-conversion-into-tax-credits-of-deferred-tax-assets-associated-with-tax-losses-carried-forward-and-other-deferred-deductions.

government this is shifting future revenue reductions all into the present, a time when government deficits are expanding significantly.

Response Options at the EU level

As the coronavirus crisis loomed increasingly large in March 2020, the European Union as well as cooperation among member states in general remained largely paralyzed,[12] unsure how to react to the situation as national governments started to close borders one after another, thus threatening the union's *Four Freedoms*—free movement of goods, free movement of capital, freedom to establish and provide services, and free movement of people—on an unprecedented level.[13] Similarly, at first, the European Central Bank seemed adamant not to get too active by first announcing that it would not cover bond spreads,[14] leading stock markets into historical doldrums.[15]

In recent weeks, however, European institutions, in cooperation with the member states, have come to the realization that EU-wide solutions are needed. With the entire union being heavily connected and interrelated to one another through the Single Market, and 19 member states further in the same boat with a common currency, demands of continent-wide responses have arisen rightfully. However, the sense to simply "do something" that currently governs discussions would be unwise. There are both good as well as bad ways to respond to the COVID-19 crisis.

Support to Mitigate Unemployment Risks and Other Relief Programs

As has been pointed out in previous sections, in the short term, economic relief for those affected most by the crisis—small businesses, workers, unemployed—is crucial instead of stimulating production that is currently prohibited in most European countries to actually engage in the economy. This is also true on the EU level.

Bearing this in mind, the European Commission has proposed the *Support to mitigate Unemployment risks in an Emergency* (SURE) program, which is "a new temporary instrument worth up to €100 billion to help protect jobs and people in work."[16]

[12] Kai Weiss, "Europe's 'solidarity' crumbles in the face of a crisis," CAPX, Mar. 19, 2020, https://capx.co/europes-solidarity-crumbles-in-the-face-of-a-crisis/.
[13] David M. Herszenhorn, "Coronavirus border controls imperil EU freedoms," Politico Europe, Mar. 16, 2020, https://www.politico.eu/article/coronavirus-border-controls-imperil-eu-freedoms/.
[14] Marcus Ashworth and Mark Gilbert, "ECB Throws Italian Bonds to the Bears," Bloomberg Opinion, Mar. 12, 2020, https://www.bloomberg.com/opinion/articles/2020-03-12/coronavirus-the-ecb-throws-italian-bonds-to-the-bears.
[15] Anne Sraders, "Dow plummets 10%, the biggest one-day drop since 1987's Black Monday," *Fortune*, Mar. 12 2020, https://fortune.com/2020/03/12/coronavirus-stock-market-drop-dow-jones-sp-500-bear-market-black-monday-1987/; n-tv, "Es herrscht Panik: Dax verliert fast 1300 Punkte an einem Tag," Mar. 12, 2020, https://www.n-tv.de/wirtschaft/der_boersen_tag/Der-Boersen-Tag-am-Donnerstag-12-Maerz-2020-article21635236.html.
[16] European Commission, "Questions and answers: Commission proposes SURE, a new temporary instrument worth up to €100 billion to help protect jobs and people in work," Apr. 2, 2020, https://ec.europa.eu/commission/presscorner/detail/en/QANDA_20_572.

The SURE program will manifest itself through loans directly from the EU to member states that are in need of financial assistance in their employment policies. Particularly, the Commission argues, it should help in setting up or extending national short-time work schemes, as we have presented in the case of Germany.

This relief scheme has several upsides in that it is promoting a successful scheme—*Kurzarbeit*—with a proven track record. It is considered “of a temporary nature” and can only be used to tackle “the consequences of the coronavirus pandemic.” While it would be better to finance the program by diverting resources of the EU budget away from other programs, borrowing the money from financial markets—as the Commission plans to do it—while asking the member states to issue guarantees of €25 billion to the Commission[17] makes the financing of the project less dubious than other ideas presented below. The decision will need the support of all member states, making it a democratic decision. And it would actually concretely help those in need while the economy is on pause, instead of simply handing out money unsystematically or making fundamental structural changes that would be difficult to revert in the long run.

Similarly, other announced relief programs will help member states cope with the crisis, such as the *Coronavirus Response Investment Initiative* with greater flexibility of using funding from the EU budget, particularly the available resources of the European Structural and Investment Funds. The scheme, which has been expanded to more flexibility of Cohesion Funds, “allows that all non-utilised support from the cohesion policy funds can be mobilised to address the effects of the public health crisis on our economies and societies.” Whereas member states were previously only able to transfer funds between regions of up to 3 percent, there is no limit anymore. No new financial resources will be needed for these immediate support programs.[18] The greater flexibility in Cohesion Funds will free up €37 billion.[19]

Ensuring Cross-Border Trade

Borders are closed both within the European Union as well as to the outside for most travel. Whereas this is temporarily understandable to contain the virus and prevent it from further spreading, it has also caused major disruptions in cross-border trade, particularly within the Single Market, where “road-travel restriction and grounded air transport threaten companies’ abilities to

[17] Paola Tamma and Lili Bayer, “Von der Leyen calls for ‘tangible’ solidarity on €100B jobs scheme,” Politico Europe, Apr. 2, 2020, https://www.politico.eu/article/von-der-leyen-calls-for-tangible-solidarity-on-e100b-jobs-scheme/.
[18] European Commission, “Questions and answers on the Coronavirus Response Investment Initiative Plus: New actions to mobilise essential investments and resources,” Apr. 2, 2020, https://ec.europa.eu/commission/presscorner/detail/en/QANDA_20_574.
[19] European Council, “Report on the comprehensive economic policy response to the COVID-19 pandemic,” Apr. 9, 2020, https://www.consilium.europa.eu/en/press/press-releases/2020/04/09/report-on-the-comprehensive-economic-policy-response-to-the-covid-19-pandemic/.

produce and deliver goods and services."[20] Endless traffic jams at borders were the norm in many parts of Europe in March, disrupting production processes and supply chains.[21]

In response, the EU has attempted to uphold cross-border trade. In regard to imports from non-EU countries, it has waived customs duties and VAT—but only on medical equipment so far.[22] This could be expanded much further to ease the burden on European businesses. The U.S. government, for instance, is mulling whether to delay tariff payments for 90 days.[23] Similarly, the EU could either defer duties or completely suspend them until lockdown measures will be lifted in general.

Despite unavoidable disruptions during this pandemic, trade barriers, full border lockdowns, or disintegrations of value chains need to be prevented.

Monetary Policy Support

While the European Central Bank under the new leadership of Christine Lagarde was first cautious to get overly active in the gradually emerging coronavirus crisis, it has since become much more intervening—potentially reinventing Mario Draghi's "whatever it takes to preserve the euro"[24] to *whatever it takes to get the European economy through the coronavirus crisis*.

First it announced that interest rates will remain unchanged at 0 percent and—when it comes to the deposit facility—even negative areas. Additional net asset purchases of €120 billion were announced as well as more favorable terms for longer-term refinancing operations (LTROs).[25] In a later decision, the ECB declared a much larger, €750 billion strong, *Pandemic Emergency Purchase Programme* (PEPP),[26] with Lagarde adding that her commitment to the euro has "no limits."[27]

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[20] Laurence Norman Drew Hinshaw, "Europe Tries to Salvage Decades of Integration as Coronavirus Shuts Borders," *The Wall St. Journal*, Apr. 14, 2020, https://www.wsj.com/articles/europe-tries-to-salvage-decades-of-integration-as-coronavirus-shuts-borders-11585301402.

[21] Barbara Moens, "The cure for the coronavirus crisis: More trade or less?" Politico Europe, Apr. 1, 2020, https://www.politico.eu/article/the-cure-for-the-coronavirus-crisis-more-trade-or-less/.

[22] European Commission, "Coronavirus: Commission waives customs duties and VAT on the import of medical equipment from non-EU countries," Apr. 3, 2020, https://ec.europa.eu/commission/presscorner/detail/en/ip_20_575.

[23] Sabrina Rodriguez, "Temporary tariff relief likely coming," Politico, Apr. 1, 2020, https://www.politico.com/newsletters/morning-trade/2020/04/01/temporary-tariff-relief-likely-coming-786568.

[24] European Central Bank, "Speech by Mario Draghi, President of the European Central Bank at the Global Investment Conference in London," July 26, 2012, https://www.ecb.europa.eu/press/key/date/2012/html/sp120726.en.html.

[25] European Central Bank, "Monetary policy decisions," Mar. 12, 2020, https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.mp200312~8d3aec3ff2.en.html.

[26] European Central Bank, "ECB announces €750 billion Pandemic Emergency Purchase Programme (PEPP)," Mar. 18, 2020, https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200318_1~3949d6f266.en.html.

[27] Reuters, "ECB's commitment to the euro has 'no limits': Lagarde," Mar. 18, 2020, https://www.reuters.com/article/health-coronavirus-ecb-lagarde/ecbs-commitment-to-the-euro-has-no-limits-lagarde-idUSF9N29R018.

The scope of the PEPP is arguably gigantic, though not necessarily unprecedented, as the ECB has engaged in previously unimaginable and loose monetary policy ever since the financial crisis of 2007—or, one might argue, over the last two decades, where the money supply has increased substantially.[28]

While immediate economic relief is dearly needed during these difficult times, lingering consequences of growing public debt (more below) or a continued monetary intervention of this size should be avoided by all means. Forcing an artificial recovery through monetary expansion would not only miss the aim of relief over stimulus, but also imperil the euro and potentially send the European economy into a much greater tailspin at a later date.

Coronabonds, ESM Credit Lines, and Debt Collectivization

No other policy proposal in recent weeks has caused as much controversy as so-called *coronabonds*, i.e., *eurobonds* that would be introduced to tackle the COVID-19 economic fallout, either temporarily—only for the time of the pandemic—or long-term.[29]

Eurobonds were already a hotly debated instrument during the euro crisis, eventually failing due to the objections of several member states. The concept is simple: a bond is issued for all Eurozone countries together instead of one for each member state, as is currently being done. In the words of Spain's Prime Minister Pedro Sánchez, in the times of this pandemic, this mutual mechanism through solidarity is essential: "If the virus does not respect borders, then nor should financing mechanisms."[30]

At least nine Eurozone members have supported the proposal so far, including France, Spain, Italy, and Portugal, whereas several others, among them most prominently Germany and the Netherlands, have rejected the idea.[31]

In a letter to European Council President Charles Michel, the nine heads of states supporting the idea argued that "we need to work on a common debt instrument issued by a European institution to raise funds on the market on the same basis and to the benefits of all Member States, thus ensuring stable long term financing. … The case for such a common instrument is strong, since we are all facing a symmetric external shock, for which no country bears responsibility, but whose negative consequences are endured by all."[32]

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[28] Martin Gundinger, "True 'Austrian' Money Supply," Austrian Economics Center, https://www.austriancenter.com/true-austrian-money-supply-tms/.
[29] See, for example, Pedro Sánchez, "Europe's future is at stake in this war against coronavirus," *The Guardian*, Apr. 5, 2020, https://www.theguardian.com/world/commentisfree/2020/apr/05/europes-future-is-at-stake-in-this-war-against-coronavirus.
[30] Ibid.
[31] Eline Schaart, "Dutch finance minister acknowledges lack of empathy on corona bonds," Politico Europe, Mar. 31, 2020, https://www.politico.eu/article/dutch-finance-minister-acknowledges-lack-of-empathy-on-corona-bonds/.
[32] See Shahin Vallée Twitter feed, Mar. 25, 2020, https://twitter.com/Shahinvallee/status/1242790458926993409.

In a more direct letter in the German daily *Frankfurter Allgemeine Zeitung*, several powerful Italian politicians also reminded Germany, after its opposition to the proposal, of their "debt" to Europe after World War II: "With the Coronavirus the common history of the West has become important again. … It is solidarity that Germany was entrusted with by many European countries after the war and until reunification. … Dear German friends, remembrance helps to make the correct decision."[33]

***Eurobonds*: A Bad Idea in the Past, a Bad Idea Now**

However, downsides to the *eurobonds* can still—like several years ago—be found in abundance. While the argument by proponents—everyone within the Eurozone has the same currency, so having the same financial instruments is the logical consequence—is daring, the major challenge is that this monetary union has never been coupled with a common fiscal union. This means that while every member state has, indeed, the same currency, they have (vastly) different fiscal policies, tax, and budget systems, without any mutual rules that are applied to all countries. (At least not practically; after all, the Stability and Growth Pact [SGP], which officially limits debt levels, has found little application).

The results from this within the Eurozone have also been starkly different. Whereas some countries like Germany, the Netherlands, Austria, and Sweden have tried to improve their balance sheets since the euro crisis,[34] other countries have instead spent more money and followed less austere policies. For instance, Italy has increased public debt since 2012, now at 135 percent of public debt to GDP (i.e., 75 percent higher than the SGP would allow), and is befallen with non-performing loans and "zombie banks."[35] Interest rates have seen a harmonization in recent years due to, among other factors, the ECB purchasing government bonds, which has reduced bond spreads. But government bonds are still demanded on different scales and prices due to the respective country's fiscal health, debt levels, and the state of the economy.

All of this would be gone in the case of *eurobonds,* where all bonds are bundled into one single euro-wide instrument, entailing both the risks as well as securities of all countries, both fiscally healthy and unhealthy. This means that those member states which have acted fiscally responsible would issue the same bonds as those that have done less so. The moral hazard that has already been created by the ESM system and the ECB's bond purchasing programs would further intensify, as it would be even easier than previously to collectivize debt, leading to even more irresponsible behavior regarding government spending.

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[33] In the letter, the Netherlands was also accused of "a lack of ethics and solidarity in all respects." See Ina D'hondt Twitter feed, Mar 31, 2020, https://twitter.com/InaDhondt/status/1244748648099000320.

[34] Dan Mitchell, "European Fiscal Crisis, Round 2?" International Liberty, Mar. 26, 2020, https://danieljmitchell.wordpress.com/2020/03/26/european-fiscal-crisis-round-2/.

[35] Desmond Lachman, "The Coronavirus Could Create A Massive EU Debt Crisis (Think Italy)," *The National Interest*, Mar. 25, 2020, https://nationalinterest.org/blog/buzz/coronavirus-could-create-massive-eu-debt-crisis-think-italy-137177.

The consequence would be twofold: for one, the incentive for a healthy fiscal policy, for keeping public debt within limits, for a sustainable economic policy, would be eliminated. Even more so, there would be a new incentive in place to borrow more, as a country receives the benefits through newly issued money, but the responsibility would weigh on all member states. It would penalize those that follow a healthy fiscal policy, and reward those who have not. While "Europeans were promised the euro would not become an excuse or vehicle for large fiscal transfers between member states," this is, in fact, what would be fully institutionalized by *eurobonds*.[36] The potential *tragedy of the commons* that some commentators[37] have seen in the eurosystem would finally fully set in.

While it has been attempted to prevent this debt collectivization,[38] so far no mechanism has been developed to fully safeguard this from eventually resulting. As a short-term policy, *eurobonds* specifically as *coronabonds* would prove futile, too, as this instrument would need the support of all national parliaments, which is, if anything, a long process, but also extremely difficult to achieve for such a contentious policy.

ESM Credit Lines

If more emergency funding next to those provided by the Commission is needed, an alternative to *coronabonds* as well as even looser monetary policy—and an alternative which member states have agreed to using as of April 9—may be found in the European Stability Mechanism (ESM), which was implemented in 2012 as a rescue mechanism for countries in difficulties. Since the structure of the ESM is already in place, funds would be quickly available. Further, it has conditionality attached to using funds, meaning those using the resources need to follow fiscally healthy policies (at least sooner or later). Current ESM funds are on-hand and can be readily used—and if all member states were to agree to it, it could be expanded if absolutely needed.[39]

Best Practices and Mistakes to Avoid

When it comes to short-term responses to the coronavirus crisis, each policy needs to be assessed on whether it would be genuine relief for economic actors rather than a stimulus. On the individual country level, the challenge is to avoid relying on temporary policy responses that will undermine longer-term growth opportunities. A temporary fiscal response that does not provide sufficient support for businesses or works against the possibility of reactivating the workforce following the health crisis would exacerbate the economic challenges that countries will face.

[36] *The Wall Street Journal* Editorial Board, "The Coronavirus Euro," Mar. 26, 2020, https://www.wsj.com/articles/the-coronavirus-euro-11585248626.
[37] For example, Philipp Bagus, *The Tragedy of the Euro* (Auburn, AL: Ludwig von Mises Institute), 2010.
[38] For example, Markus K. Brunnermeier et al., "ESBies: Safety in the tranches," European System of Financial Supervision: Working Paper Series, No. 21, September 2016, https://www.esrb.europa.eu/pub/pdf/wp/esrbwp21.en.pdf.
[39] Matthias Kullas and Bert Van Roosebeke, "Combating the Corona crisis: Economic and fiscal policy recommendations," cepInput: no. 8, https://www.cep.eu/en/eu-topics/details/cep/bewaeltigung-der-corona-krise-cepinput.html.

The EU's rule in this is often also to simply point out best examples, but otherwise to give room to its member states to pursue their plans, equipped with the necessary on-ground knowledge that is needed for this crisis. Under this light, the temporary suspension of the SGP is a wise decision.[40] Helping those hurt by the virus and the decreed lockdowns while the economy is on hold will naturally mean to take on more debt—for now.

The direct economic relief through SURE and by reshuffling the Cohesion Funds is also fulfilling the need for concrete policies that support those vulnerable at the moment, similar to all attempts to keep the free movement of goods as well as trade with non-EU countries going. If the situation worsens significantly, the ESM credit lines could be activated to increase financial resources for those countries particularly hit.

However, this crisis cannot be an excuse to implement bad policies through the backdoor, under the mantle of this trauma. Both *eurobonds* as well as ultra-loose monetary policy would hurt the European economy in the medium- to long-term and send wrong signals. In the short term, support is needed. But this does not translate to damaging policies that would stick forever.

While the sentiment of simply "doing something" is understandable, every policy still needs to be examined on genuinely rational grounds. If this is done, it turns out, bad policies from the past remain bad policies for the present.

Long-Term Policies

The health response and the economic shutdown due to the crisis should allow for the pandemic to eventually subside. When it is safe to reopen the economy, some sectors will likely open faster than others. Businesses that lay off employees will need to spend time either rehiring those former workers or recruiting new workers. The crisis itself could change the economics for some business sectors, and it may be more common for employees to work remotely in the future.

Though those outcomes are uncertain, the need for an economic rebound after the crisis subsides is certain. The fiscal response to the crisis will increase debt and deficit levels and growth will be necessary for tax bases to cover at least some of those costs. While the current fiscal policies are designed to be temporary, long-term policy measures to return to growth and sustainable public finances should be considered.

There are challenging forces at play. The first is the potential for a sovereign debt overload in the countries most impacted by the crisis. Countries will need to avoid allowing a debt crisis to follow

[40] Jorge Valero, "EU countries warn of 'severe economic downturn,' suspend Stability Pact," EURACTIV, Mar. 24, 2020, https://www.euractiv.com/section/economy-jobs/news/eu-countries-warn-of-severe-economic-downturn-suspend-stability-pact/.

the health crisis. The second force, for Eurozone countries, is the eventual pressure for fiscal tightening following the downturn.

Even with a pro-growth tax policy mix with a wide consumption tax base, income taxes that allow businesses to deduct costs of investments and do not penalize individual savers may not produce enough revenue in the short term to cover the costs of this crisis. So it is important for countries to consider the least harmful ways of reaching sustainable public finances. Eurozone countries should also consider ways to collectively avoid a European debt crisis as well as ways to minimize the likelihood of near-term austerity policies.

Long-Term Responses at the Country Level

The sizable fiscal response to the crisis alongside the economic shutdown will create incredible pressures on government revenues. During the Great Recession, tax revenues fell by 11 percent from 2008 to 2009 among OECD countries.[41] Spending increases paired with collapsing revenues chart a collision course for Eurozone countries with European fiscal rules. This crisis will be the first real test of the so-called six and two-pack reforms that strengthened the monitoring of public finances in Europe during and after the crisis. The European Commission has already identified the *general escape clause* as applying to the current crisis.[42] This escape clause loosens European fiscal rules due to a “severe economic downturn in the euro area or the Union as a whole.”

While the fiscal rules are loosened for the time being, policymakers should be cautious when determining when the rules should snap back into place after the crisis. The EU should identify a clear metric for returning to enforcement of fiscal discipline mechanisms. Given that the escape clause has been triggered by a crisis felt by countries across the Union, deactivating the clause should be triggered by EU-wide growth. That trigger could be, for instance, two consecutive years of 2 percent growth paired with a forecast of sustained growth at that level for the following year. That design or a similar threshold would provide flexibility in dealing with the crisis at hand and the economic challenges to follow. Individual countries should be given similar flexibility within the context of country-specific fiscal evaluations once the EU-wide exception to fiscal rules no longer applies.

When the fiscal rules and associated penalties and sanctions for violating them do return, policymakers should be careful when designing policies to meet fiscal targets. Lessons from the fiscal consolidation following the great recession should be heeded.

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[41] Daniel Bunn, “Tax Policy and Economic Downturns,” Tax Foundation, Mar. 18, 2020, https://taxfoundation.org/government-revenue-most-hit-recession/.

[42] European Parliament Think Tank, “The 'general escape clause' within the Stability and Growth Pact: Fiscal flexibility for severe economic shocks,” Mar. 7, 2020, https://www.europarl.europa.eu/thinktank/en/document.html?reference=EPRS_BRI(2020)649351; and European Fiscal Board, “Assessment of EU Fiscal Rules,” August 2019, https://ec.europa.eu/info/sites/info/files/2019-09-10-assessment-of-eu-fiscal-rules_en.pdf.

The OECD has highlighted that economic growth helps reduce budget deficits and control debt ratios as it boosts tax revenues and reduces unemployment spending. It will thus be important to ensure that tax policies do as little harm as possible to drivers of output and employment growth—such as incentives to work, save, and invest—while generating sufficient tax revenue.[43]

Evidence shows that some taxes are more distortive than others, impeding economic growth to a greater degree. Corporate income taxes can be particularly harmful to economic growth as they can disincentivize business investments, a central driver of economic growth. High personal income taxes can have a negative impact on the decision to work which, in turn, can also negatively impact economic growth.[44]

Consumption taxes, such as the VAT, do not have a direct effect on the incentive to work or invest, making them less harmful to economic growth. Taxes on immovable property are also known to have relatively little impact on growth.[45]

In terms of pro-growth tax policy, Europe is home to both the best and worst tax systems among developed countries.[46] Estonia and Latvia have cash flow taxes on businesses and significant consumption taxes. France, Italy, and Spain, on the other hand, have multiple layers of taxes that can create economic distortions and harm the efficiency of revenue collections.

Counterproductive tax hikes, adopted in the name of deficit and debt reduction, can lead to longer-term losses in output.[47] Instead of pursuing policies that could negatively impact business investment and longer-term public investment projects, countries should focus on making current spending levels temporary and broadening tax bases in ways that limit the harm to long-term growth prospects.

Focusing on Growth and Sustainable Revenues

Countries should recognize that the necessary revenues to support spending programs should be derived from tax bases that are not prone to volatility. This is already the case for many countries in Europe, with broad reliance on VAT revenue. Additionally, policies that support employment and business investment should be implemented.

All of Europe should take some tax policy lessons from the Baltic countries which, relative to the rest of Europe, have simple direct taxes and broad indirect taxes. Estonia, Latvia, and Lithuania

[43] OECD, "Tax Policy Reform and Fiscal Consolidation," December 2010, https://www.oecd.org/tax/tax-policy/46600079.pdf.
[44] OECD, "Tax Policy Reform and Economic Growth," 2010, https://read.oecd-ilibrary.org/taxation/tax-policy-reform-and-economic-growth_9789264091085-en#page1.
[45] Ibid.
[46] Daniel Bunn and Elke Asen, *International Tax Competitiveness Index*, Tax Foundation, 2019, https://taxfoundation.org/publications/international-tax-competitiveness-index/.
[47] Salim Furth (ed.), "Europe's Fiscal Crisis Revealed: An In-Depth Analysis of Spending, Austerity, and Growth," The Heritage Foundation, Special Report No. 147, June 6, 2014, http://thf_media.s3.amazonaws.com/2014/pdf/SR147.pdf; and Antonio Fatás and Lawrence H. Summers, "The Permanent Effects of Fiscal Consolidations," National Bureau of Economic Research, NBER Working Paper 22374, June 2016, https://www.nber.org/papers/w22374.pdf.

rank highly on the Tax Foundation's *International Tax Competitiveness Index* for these reasons, and other European countries should follow that model.

The design of corporate taxes in many countries across Europe penalizes business investments, and countries should adopt policies that support new investments as part of a post-crisis growth policy.[48] This is especially critical because investment as a share of GDP has been weak across Europe and is still below 2007 levels.[49]

VAT systems across Europe are also ripe for change. The estimated VAT gap in 2017 was €137.5 billion.[50] This revenue is lost due to fraud, bankruptcies, and poor administration of VAT systems. Addressing this revenue shortfall with strengthened enforcement and technological solutions would be valuable.

The VAT gap is not the only challenge with indirect taxation in Europe. Throughout Europe, countries provide carveouts from VAT for various goods and services and provide special, lower rates for other categories. These policies can distort consumption behavior and increase challenges for VAT administration.[51] A VAT system with numerous carveouts or special-rated goods and services requires a higher standard rate to raise revenue than otherwise. One measure of this is the VAT revenue ratio which shows that, among OECD countries with national consumption taxes, just 60 percent of final consumption is covered by current VAT.[52]

Both better administration of VAT policies along with base broadening could provide substantial revenues to meet fiscal goals without creating unnecessary barriers to investment and savings.

Long-Term Responses at the EU Level

Demands for a European *Marshall Plan* have been flaring up in discussions of the long-term responses to the coronavirus crisis. Commission President Ursula von der Leyen has talked about a *Marshall Plan* that "we are laying out together as a European Union for the European people."[53] In similar terms, Spanish Prime Minister Pedro Sánchez has called for "a wartime economy" with "European resistance, reconstruction, and recovery." After the health crisis is over, Europe would

[48] Elke Asen, "Capital Cost Recovery across the OECD," Tax Foundation, Apr. 8, 2020, https://taxfoundation.org/capital-cost-recovery-across-the-oecd-2020/.
[49] 21.2 percent in 2019 vs. 22.5 percent in 2007. See Eurostat, "How much does your country invest?" May 14, 2018, https://ec.europa.eu/eurostat/web/products-eurostat-news/-/DDN-20180514-1.
[50] Directorate General Taxation and Customs Union, "Study and Reports on the VAT Gap in the EU-28 Member States: 2019 Final Report," IHS, Institute for Advanced Studies, Sept. 4, 2019, https://ec.europa.eu/taxation_customs/sites/taxation/files/vat-gap-full-report-2019_en.pdf.
[51] Max Sjöberg, "En miljard för differentierad moms," Timbro, Briefing Paper 26, Mar. 19, 2020, https://timbro.se/ekonomi/skatter/en-miljard-for-differentierad-moms/.
[52] Hannah Simon and Michelle Harding, "What drives consumption tax revenues?" OECD Taxation Working Papers, No. 47, Apr. 2, 2020, https://www.oecd-ilibrary.org/taxation/what-drives-consumption-tax-revenues_94ed8187-en.
[53] Paola Tamma and Lili Bayer, "Von der Leyen calls for 'tangible' solidarity on €100B jobs scheme."

need to “rebuild the continent’s economies by mobilising significant resources through a plan we are calling the new Marshall plan.”[54]

The idea behind a European *Marshall Plan* is straightforward: after World War II, Europe recovered due to the support by the United States, which offered the necessary resources to rebuild the continent’s economy. After the COVID-19 crisis, a similar spending spree could elevate the EU’s economy out of its current problems. There are, however, many problems with this view, which should make us skeptical of this solution.

For one, while COVID-19 will have substantial effects on the economy, it is not a war with the death toll of World War II or the incredible destruction of physical capital.

Furthermore, the measures through which such a *Marshall Plan* would come into being would prove problematic too. Once more, we would find ourselves in the situation of simply wanting to “do something,” suddenly considering options that were previously deemed unviable or economically damaging.

The main instrument for a *Marshall Plan* would be the next Multiannual Financial Framework (MFF) for the period of 2021-2027.[55] As Ursula von der Leyen has said, “I think the European budget should be the Marshall Plan.”[56] The April 9 agreement by member states also argued that the MFF “will play a central role in the economic recovery.”[57]

The negotiations for the upcoming MFF would have been the decisive debate on the EU level this year if it weren’t for COVID-19, paving the way on the future direction of Europe. But throughout the last months and, at this point, years—ever since the Juncker Commission presented its first proposal in May 2018[58]—more and more disagreements have arisen between member states.

The so-called Hanseatic League 2.0 around the Netherlands, Sweden, Denmark, and Austria wanted a smaller budget post-Brexit. Others, like France, Italy, and Spain advocated for a bigger budget so as to realize bigger projects on the EU level. Even within the group of those countries that wanted to expand the budget, there was little consensus: some demanded that agricultural

[54] Pedro Sánchez, “Europe’s future is at stake in this war against coronavirus.”
[55] The other possible instrument discussed so far is a Recovery Fund, though no details are available yet on how this fund would precisely look. However, the Executive Vice President for the Economy of the European Commission, Valdis Dombrovskis, has estimated the size to be around €1.5 trillion, the funding extracted from financial markets. This would be another stimulus program that this paper has considered unwise for a sustainable economic recovery. See Ruth Berschens, “’Schlimmer als nach der Finanzkrise’ - EU plant billionschweren Wiederaufbaufonds,” Handelsblatt, Apr. 14, 2020, https://www.handelsblatt.com/politik/international/coronakrise-schlimmer-als-nach-der-finanzkrise-eu-plant-billionenschweren-wiederaufbaufonds/25736696.html.
[56] Pedro Sánchez, “Europe’s future is at stake I this war against coronavirus.”
[57] European Council, “Report on the comprehensive economic policy response to the Covid-19 pandemic,” Apr. 9, 2020, https://www.consilium.europa.eu/en/press/press-releases/2020/04/09/report-on-the-comprehensive-economic-policy-response-to-the-covid-19-pandemic/.
[58] Kai Weiss, “Brussels still refuses to face up the fiscal reality of Brexit,” CAPX, May 2, 2018, https://capx.co/brussels-still-refuses-to-face-up-the-fiscal-reality-of-brexit/.

subsidies would not be reduced, others wanted to see Cohesion Funds increased. The new von der Leyen Commission instead proposed to use resources on the European Green Deal and a European industrial strategy. Before the coronavirus swept over Europe, a summit on the EU budget at the end of February proved only that opinions were (very) far apart.[59] And these disagreements will not simply vanish with calls for a *Marshall Plan*—they will likely, if anything, widen if a much larger budget is in the minds of some.

And a much larger budget would be needed for a *Marshall Plan*. The assistance that the U.S. provided to European countries from 1948 to 1952 was $13.2 billion, or the equivalent of 2.6 percent of economic output of the 16 European recipients (significantly less than the current 27 EU member states).[60] The Commission's original proposal for the upcoming MFF was only 1.11 percent of Gross National Income—and after the many disagreements, this was even reduced to 1.07 percent.

Lastly, there is significant doubt whether the *Marshall Plan* was actually responsible for Europe's recovery. As Tyler Cowen has noted, "At best, its effects on postwar Europe were mixed," and in most successful recoveries, economic growth "was encouraged by European leaders themselves, such as West Germany's Ludwig Erhard and Italy's Luigi Einaudi."

Indeed, finds Cowen, if anything, the *Marshall Plan* era showed that "sound economic policy is by far the most important factor in economic growth."[61] And as in the case of Germany under Konrad Adenauer and Ludwig Erhard, this sound economic policy was exemplified by pro-market, free-trade reforms, healthy public finances, and sound money.[62] That is, a sustainable recovery was the reason for Germany's upheaval after its post-war destruction.

Safeguarding and Expanding the Single Market

One of the most effective ways—and perhaps the most palatable European-wide way—for a sustainable recovery after the coronavirus is to ensure Europe's *Four Freedoms* are oriented at fastening wealth creation, and to use the still unutilized opportunities of the Single Market as well as free trade with the outside world.

Questions have arisen in the wake of COVID-19 whether free trade is still a good avenue to move forward.[63] There are important questions that need to be asked, and whether some production—

[59] Lili Bayer, "EU budget summit ends with no deal," Politico Europe, Feb. 21, 2020, https://www.politico.eu/article/eu-budget-summit-ends-with-no-deal/.
[60] Lili Bayer, "EU budget won't be corona-era Marshall Plan," Politico Europe, Apr. 6, 2020, https://www.politico.eu/article/reality-check-marshall-plan-for-europe-coronavirus-ursula-von-der-leyen/.
[61] Tyler Cowen, "The Marshall Plan: Myths and Realities," In Doug Bandow, *U.S. Aid to the Developing World: A Free Market Agenda* (Washington, D.C.: Heritage Foundation) 1985, 61-74.
[62] Kai Weiss, "Is Germany Successful Thanks to Socialism?" In Lawrence W. Reed (ed.): *The XYZ's of Socialism* (Atlanta, Georgia: Foundation for Economic Education), 1985, 244-255.
[63] See, for example, David Goodhart, "Farewell free trade, and good riddance," UnHerd, Mar. 6, 2020, https://unherd.com/2020/03/its-time-liberals-embraced-economic-nationalism/.

for example, of pharmaceutical products—should be brought home to Europe.[64] Also, the risks of trade with China need to be reevaluated in the response to this crisis.[65]

Nonetheless, free trade is still one of the most effective wealth creators in existence, and the European Single Market has been a great boon for the European economy. According to the European Commission, through the Single Market, 56 million jobs have been created and 8-9 percent has been added to the EU's GDP—"the gain from the single market for EU Member States amounts to about €427 billion per year."[66]

At the same time, the common market is far from finished, with many trade barriers still being in place. If the EU were to integrate the market even more, this could generate an additional €183-269 billion annually for manufactured goods, and €338 billion annually for services, "together raising EU GDP by approx. 12%." Thus, "the benefits of removing the remaining barriers to a fully functioning single market for goods and services could amount to €713 billion by the end of 2029."[67]

Further economic gains could be achieved by new free trade agreements with non-EU countries like Australia, New Zealand, the Mercosur countries, and the U.S. as well as making permanent some tariff reliefs on imports (as presented in the section on short-term solutions). There could hardly be a better and easier way to help Europe's economy out of the slump.

Reinforcing the Importance of Fiscal Health

The Stability and Growth Pact—which limits public debt of member states to 60 percent of GDP and deficit levels to 3 percent of GDP—has been suspended since March 23 after a *general escape clause* was agreed upon by member states. As we have noted, this was a necessary decision to enable economic relief programs during this crisis and while the lockdown measures are in place. However, after the virus has subsided, a return to fiscally healthy policies needs to be targeted as soon as possible.

Indeed, a reinforcement of the SGP, which has taken on a more theoretical form in recent years as many countries ignored it, will be dearly needed. After the crisis, public debt and government deficits will have further ballooned after national liquidity measures and relief schemes by national governments as well as Commission programs of at least €2.77 trillion have been introduced.[68]

[64] Barbara Moens, "The cure for the coronavirus crisis: More trade or less?"
[65] Shadi Hamid, "China Is Avoiding Blame by Trolling the World," *The Atlantic*, Mar. 19, 2020, https://www.theatlantic.com/ideas/archive/2020/03/china-trolling-world-and-avoiding-blame/608332/; and David Harsanyi, "COVID-19 Is the Chinese Government's Curse upon the World," *National Review*, Mar. 17, 2020, https://www.nationalreview.com/2020/03/covid-19-is-the-chinese-governments-curse-upon-the-world/.
[66] European Commission, "A single market that delivers for businesses and consumers," Mar. 10, 2020, https://ec.europa.eu/commission/presscorner/detail/en/fs_20_427.
[67] Ibid.
[68] The numbers are from April 7, 2020. European Commission, "Coronavirus response: Economy.".

When the European economy is on track for sustainable growth again—for instance, through the methods described above of reinstating the SGP—it will be time to cut government spending, subsidy and state aid programs, and prevent massive stimuli. The opposite would merely extract resources out of the private economy, put an unnecessary burden on businesses and individuals, and, in the case of increasing debt, would delay payment day into the future and onto the back of the next generations—not even to mention the increased dangers of an economic crisis in the medium to long run when governments in a particularly bad fiscal position would have a difficult time to prevent bankruptcy.

Tax Policy for Growth, No Universified Taxation

Finally, in accordance with fiscal responsibility, the tax burden should be designed to support economic growth. In previous chapters, we have taken a look at good options for a sound, broadly applied, neutral tax system with a lower burden on taxpayers. The European Commission can identify good practices and promote those around the continent.

However, this does not translate into a call for a more centralized tax system. Tax harmonization on the EU level would attack the ability for member states to pull themselves out of the crisis and eliminate the trial-and-error process which makes the identification of best practices possible in the first place. The competitive factor among tax systems in Europe has also incentivized political leaders to pursue better and less-burdensome taxation.[69]

Policies that have been discussed recently could create setbacks for Europe during an economic recovery. The discussion of an EU Financial Transactions Tax continues to ignore the problems that such a tax would create for capital markets and investors.[70] Similar discussions of an EU-wide wealth tax would be detrimental to post-crisis opportunities for growth.[71] A temporary wealth tax designed to coincide with a new EU financing mechanism would arguably combine two challenging implementation problems into one.[72]

It is likely that countries in Europe will also continue to argue for an EU solution to digital taxation. Digital services taxes are now proliferating across Europe, but now is the time for countries to reconsider how such narrow taxes fit with sustainable public finances. Designing tax policy around a particular industry, even if that industry is currently flourishing, could have detrimental impacts down the road. Europe already lags behind in investment by technology companies, and continuing a policy that is harmful to those businesses would be shortsighted.[73]

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[69] Kai Weiss, "Tax Competition: A Practical Way to a Low-Tax World," Sept. 22, 2018, https://www.austriancenter.com/tax-competition/.

[70] Colin Miller and Anna Tyger, "The Impact of a Financial Transaction Tax," Tax Foundation, Jan. 23, 2020, https://taxfoundation.org/financial-transaction-tax/.

[71] Huaqn Li and Karl Smith, "Analysis of Sen. Warren and Sen. Sanders' Wealth Tax Plans," Tax Foundation, Jan. 27, 2020, https://taxfoundation.org/wealth-tax/.

[72] See Camille Landais, Emmanuel Saez, and Gabriel Zucman, "A progressive European wealth tax to fund the European COVID response," Vox.eu, Apr. 3, 2020, https://voxeu.org/article/progressive-european-wealth-tax-fund-european-covid-response.

[73] Daniel Bunn, "European Tech Firms Have Low Levels of Capital Spending," Tax Foundation, Oct. 31, 2018, https://taxfoundation.org/european-tech-firms-low-levels-of-capital-spending/.

At the EU level, calls may return to the Common Consolidated Corporate Tax Base proposal, a plan to unify some aspects of business taxation across Europe. As it stands now, the proposal has design flaws that render it to be a less competitive corporate tax system than is currently being used in many EU countries.[74] Simplifying corporate tax rules across the EU may be beneficial, but unifying policy should not undermine the pro-growth features of many tax systems in Europe.

Conclusion

Pursuing a sustainable recovery after the effects of the coronavirus have slowed is of the utmost importance. Sustainable, however, does not translate into any unrealistic, grandiose *Marshall Plan* programs. Instead, in the long term, fiscal health needs to be restored by keeping deficits and debt in check. Pro-growth tax policies can play an important role in such long-term reduction of public debt, as well as in the overall economic recovery. For instance, broadening the base of consumption taxes and reducing the VAT gap can raise revenue without being particularly harmful to economic growth.

On the EU level, trade barriers both within as well as to the outside of the Single Market should be further reduced to fully make use of the benefits of economic liberalization and unhindered cross-border trade. Thus, the recovery could occur not through fiscally and economically unsound policies, but by economic participants enabling the (positively) disruptive, innovative effects of the market economy and of European-wide cooperation.

	Short-Term	Long-Term
National Governments	• delays or deferrals of tax payments • targeted tax credits and reductions • direct, concrete fiscal relief to those most affected	• pro-growth tax policies • lowering tax burden on labor • broadening consumption tax bases • preventing short-sighted fiscal stimulus
European Union	• ensuring cross-border trade, suspending duties • providing temporary, concrete financial support • activating ESM credit lines if needed • no eurobonds or looser monetary policy	• enforcing fiscal rules after adjustment period • deepening the Single Market • pursue free trade with world • avoid centralized tax policies that undermine pro-growth initiatives by Member State • abstain from *Marshall Plan*

Summary of the Road Map of Economic Recovery

[74] Elke Asen, "Capital Cost Recovery across the OECD."

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