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The current own resource system of the EU Budget

Still a working model for the European Union?

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Abstract

With the adoption of the new financial perspective for the years 2007 – 2013 in May 2006 the EU secured their financial planning for the next years. During this seven year intervals it, especially before a new decision is needed, discussions about rationality of the EU own resources system come up and following promises from politicians to reform it.

Evaluating the outcome of the Agenda 2007, the British rebate has slightly modified, the exemptions for other big net-paying countries increase, the assessment for the VAT resource gets even more complicated, no substantial change in the biggest spending categories and rigorous decreases in the budget categories facing the supranational duties of the EU.

Therefore this thesis will provide a general introduction into the own resources system, an overview about budget functions and criteria. Ongoing the thesis provides an overview about the changes made with the newly agreed financial perspective before reform options within the current own resources system and completely new ways for funding the budget will be discussed.

Content

List of abbreviations

GNI	Gross national income
GDP	Gross domestic product
EU	European Union
ECSC	European Coal and Steel Community
EEC	European Economic Community
VAT	Value added tax
ECB	European Central Bank
UK	United Kingdom
EP	European Parliament
CAP	Common Agricultural Policy

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Introduction

In December 2005 the EU summit agreed on a new financial perspective for the years 2007 – 2013. The negotiations between the proposals from the Commission and the proposal by the biggest six net payer countries[1] were complicated, as there was a big gap concerning the volume of the budget. In a final attempt to solve the crisis a compromise was adopted during the Council Presidency of the United Kingdom that suggested an overall volume of 862 billion Euros, round about 1.045% of the EU GNI, for the seven year period.[2] As the parliament has a right to co-decide on the budget they reached a final volume of 864.4 billion Euros and a slightly increased flexibility regarding the spending.[3]

The negotiation process should have started officially in 2004, the Commission published her budget projection in June 2003 with a volume of 1.025 billion € reaching nearly the maximum budget limit of 1.24% agreed on years ago. As a reaction the six biggest net-payers wrote a letter declaring that there is no clearance for such a volume and that the limit should be 1% of the EU GNI for the future financial perspective.[4] So before the official start of the negotiation a conflict seemed to be inescapable. Already here it is visible that there are at least two different approaches concerning the budget. The Commission comes to the fore with a focus on fulfilling the fiscal tasks according to the treaty commitments, whereas the member states, mainly the net-payer are focussed on their contributions to the budget. The second approach is limiting the budget with the consequence that individual member state interests are the main factor for the budget and not the given tasks to reach the commonly set goals.[5] Apart from the scientific discussion about the net-balance mentality that limits wanted changes in EU politics,[6] you will

[1] Germany, UK, Netherlands, Sweden, France and Austria
[2] Cp. Begg, Ian and Friedrich Heinemann (2006) : New Budget, Old Dilemmas
[3] Cp. N. N. (2006) : Deal reached on EU budget 2007-2013
[4] Cp. Becker, Peter (2006): Fortschreibung des Status Quo – Die EU und ihr neuer Finanzrahmen Agenda 2007, p. 116.
[5] Cp. ibid: p. 115.
[6] Cp. ibid: p. 121.

find criticism about the current system not only from groups standing outside of the decision process. The compromise agreed on contain a special clause that already in 2009 a comprehensive review is scheduled to discuss possible changes on the income as well on the outcome side of the EU budget.[7]

Main research question

Based on the ongoing discussion about reforming the budgetary process of the EU this thesis will concentrate on a special issue of the process: The own resources system. The own resources system, consisting of multiple sub-categories, are the main income source within the EU budget[8] besides income from tax-deduction of EU appointees, remaining money from the previous budgetary year and various other small resources. Within the system there are a number of exemptions for several member states, this result in adjustment payments of the other states, making the system intransparent and unequal. This leads to more and more new demands of exemption making the budget focus only on redistributive aspects, instead of concentrating on allocative measurements based on policy goals.[9] Therefore the main research question is:

How can the system of the own resources reformed to reach a more rational, transparent and equal system for funding the EU budget?

To answer the research question there will be several sub-questions illuminating different issues concerning the main research question.

1. How did the own resources system develop historically?
2. What are economic requirements making a budget more rational, equal and transparent?
3. What changes are implemented with the new multi annual framework 2007 – 2013?
4. What are reform options within the existing own resources system?

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[7] Cp. Becker, Peter (2006): Fortschreibung des Status Quo – Die EU und ihr neuer Finanzrahmen Agenda 2007, p. 119.

[8] According to the budget plan 2006 the own resources contribute 108 billion € and the other resources altogether less than 4 billion €

[9] Cp. Begg, Ian and Friedrich Heinemann (2006) : New Budget, Old Dilemmas

5. What are alternative options in funding the EU budget?

Structure

The thesis is divided into five subchapters each of them dealing with a special issue to answer the main research question.

Chapter one gives a comprehensive, descriptive overview about the historical development of the own resources system, when each of them was introduced how the mode of calculation is and in which way member states are targeted.

Chapter two will contain an analysis of budget functions and criteria related to equality, rationality and transparency. Besides from a theoretical financial background the criteria will be used to measure and identify the level of inequity as well as lacks of transparency.

Chapter three contain the analysis of the actual financial perspective. What will be reformed with the new perspective on the income side as well as on the expenditure side? Is the own resource system becoming more rational and transparent with this decision?

Due to the earlier analysis chapter four will raise issues of possible reform steps within the current own resource system. With the approved financial perspective there are made small steps to more equality concerning the rebate of the UK, but there are lot of other compensation mechanisms where it is questionable if they are justified and rational. The financial perspective and the negotiating process are not part of EU primary law, so there is no formal mode based on a treaty; it is informal between the decision makers. As seen in the last negotiation round, the EU meeting of the heads of state and government came so late to a decision that the parliament's right to co-decision is limited as a refusal to the financial perspective would have made it impossible to agree on a new one in time, so evaluating the decision making process is made.

In the final chapter ways towards a complete new income system will be discussed. During the years several propositions were made around the question if any kind of taxation should be transferred to the supra-national level excluding the Council and the heads of state and government from the decision making process on the income side. A main point here is if a potential EU tax is realistic and in which mode such a tax could be established and collected.

After finishing all chapters the main findings and conclusions will be summarised at the end of the thesis.

Methodology

The thesis will be based completely on desk research. This contains as primary sources: all primary and secondary law of the EU concerning the budget process as well as the budget itself and other available data from the responsible commissioner and the department. For evaluating and analysing the budgetary process and discussion the reform options secondary data is necessary. This includes recent newspaper articles, scientific articles and books, statistical data from economic institutes.

A framework for evaluating the criteria of equality and transparency will be created and the results will influence the discussion of different reform options.

For a better comprehension visualising effects like tables and diagrams will be used to present statistical data in an appropriate way.

1. The own resources system of the EU

In this chapter the historical overview about the different ways of funding the EU budget and the forerunner organisations will be given. The question at this is how the deciding institutions reacted on upcoming financial difficulties during the years and how easy or not new arrangements were found? The overview will demonstrate the adjustments between the different sources during the five own resources decisions up to the current system and their effects on the member states.

1.1 Historical overview

The financial system of the European Coal and Steel Community was based on a simple value added production tax, to be paid by the companies directly to the High Commission.[10] The foundation of the European Economic Community and the European Atomic Energy Community with the Treaties of Rome in 1957 and the Merger Treaty established a bigger financial system as spending sources were broader than administrative costs compared to the ECSC. In the beginning the budget was financed by contributions of the six member states. There were distribution keys for different spending categories, as administrative costs, investment and science costs. The distribution keys were the result of negotiations between the member states, oriented on indicators as GNP, population size and political conditions.[11]

The Contribution system was regarded as a temporary system, as Article 201 of the EEC-treaty states: *"The Commission shall study the conditions under which the financial contributions of Member States provided for in Article 200 may be replaced by other resources of the Community itself…"*[12] Therefore a first own resources decision was made in 1970. The first pillar of the introduced own resources were the ab-

[10] As the ECSC treaty phased out in 2002 there is no further relevance for the thesis.
[11] Euler, Markus (2005): Ansatzpunkte für eine Reform des Finanzierungssytems der Europäischen Union, p. 29.
[12] EEC treaty

sorption on products within the frame of the Common Agricultural Policy as e.g. on the sugar market organisation. These revenues flowing into the EU budget since 1971. A second pillar is the revenue from customs. The European customs union, existing since 1968, has a common duty on products imported; these revenues were transferred to the budget progressively increasing between 1971 and 1975 when all revenues went to the EU budget. To avoid an unbalanced budget a third source was needed, therefore the VAT based payments were installed. Originally planed from 1975 it took until 1979 as an earlier introduction was not possible, due to the lack of a common assessment base.[13] During this time provisional shares were paid by the member states to balance the budget.

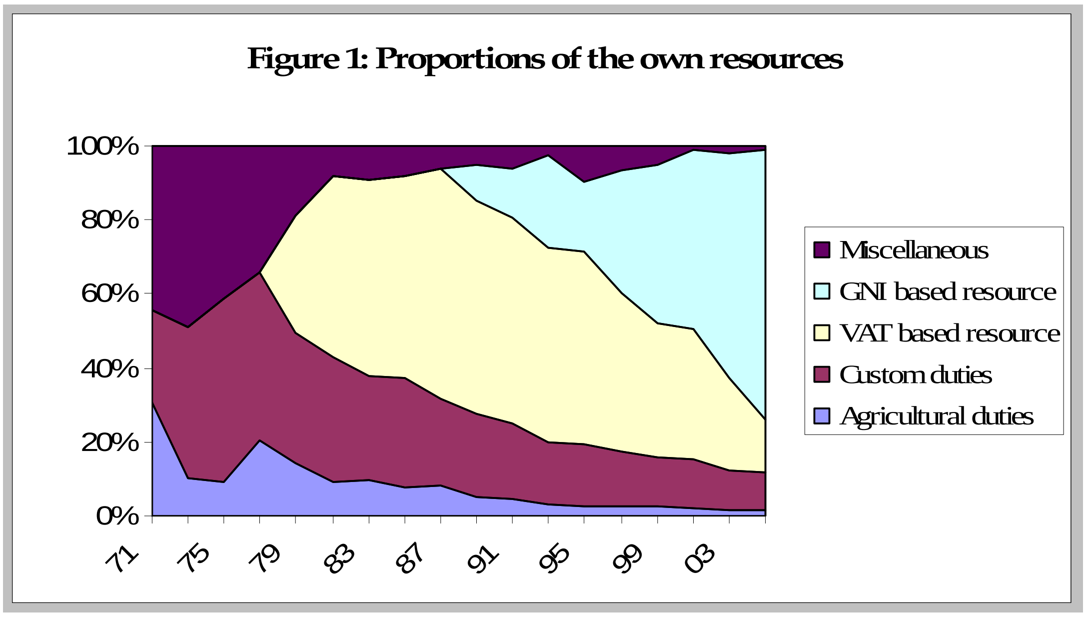
Further important points are the own resources decision of 1985 with the introduction of the so called "British-rebate" which will be discussed later in detail. In 1988 a new decision was made thus the funding of the budget was not sufficient. The major change was the introduction of a new own resource, the GNI payments. The GNI payments displace the VAT payments as rest funding tool within the budget. Apart from adjustments for special problems of particular member states that will be mentioned in the following part, the system has not gone through a substantial reform. The latest financial perspective will be regarded separately in the second chapter.

1.2 Development of the various own resources

As seen above there are different own resources playing a more or less important role for the EU budget over the years. All own resources have been modified after their introduction to react on specific problems in a particular member state. In the first years the "traditional own resources" of agricultural und custom duties were the major sources until the VAT based resource was added. After discussions about the equality of a VAT based resource, finally the GNI based resource was introduced, growing over the years and today by far the most important revenue source for the EU budget. In the following the mode of calculations as well as ex-

[13] Euler, Markus (2005): p. 32.

emptions and their impacts on the budget will be described in detail up to the state of the Agenda 2000.



Source: various data from the Commission[14]

1.2.1 Agricultural and custom duties

The agricultural und custom duties are often called "traditional own resources" as their imposition is clearly linked to the customs union. Agricultural und custom duties played in the beginning an important role for the funding of the budget, but as spending expanded the traditional own resources were insufficient. A problem with these resources is that they are fluctuating with the development of the world market and other factors, so a constant reliability is not given. These duties are collected by the member states and then transferred to the EU. In the beginning the collecting member state get a reimbursement of 10% of the amount back, later it changed and the member states only transferred 90% to the EU to avoid an artificial enlarged budget. With the Agenda 2000 and the financial year 2001 the member states remaining 25% of the traditional own resources as allowance for their

[14] EU budget 2005, 2003 and Vademecum 2000

administrative work.[15] As the amount of duties varies with the geographic location and the infrastructure of the country there are effects that lead to a indirect rebate, in this case mainly for the Netherlands and also Belgium. The ports of Rotterdam and Antwerp handle a big part of products sold in the entire EU so the Netherlands and Belgium (as well as every other member state) can retain 25% of the duties. The real administrative costs are lower so there is a windfall gain, called the Rotterdam / Antwerp effect.[16]

1.2.2 VAT based resource

The VAT based resourced was approved in 1970 with an original introduction date of 1975. The calculation was far more complicated in contrast to the traditional resources, but it was needed as the two first resources were not sufficient for funding an enlarging budget and could not be aroused unlimited.[17] On of the problem is the different level of the VAT tax in the different member states. As a tax harmonisation was not possible they agreed on a harmonisation of the assesement base. The assessment is measuring the consume activities in the member states and based upon this they pay the quota needed to balance the budget.[18] There was also a ceiling originally 1% of the assesement base value. The own resource decision of 1985 brought major chances for the VAT based resource. The most important one is the so called "British-rebate" which is a compensation of 66% of the difference between the VAT based amount paid by the UK and the money received from the EU. The lack of money has to be paid by the other members, whereas Germany got the exemption to pay only 67% of the enhanced contribution. As spending increased fast due to the accession of Spain and Portugal with a significant agricultural sector, already three years later the next own resource decision brought the major change introducing the GNI based resource.

The VAT assessment base is from now on linked to the GNI and will only be regarded to the amount of 55% of the GNI as countries like Spain made clear that

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[15] Cp. Euler Markus (2005) : p.31.
[16] Begg, Ian (1999): Reshaping the EU Budget: Yet Another Missed Opportunity, p. 8.
[17] Cp. Ibid: p. 4.
[18] Cp. Euler, Markus (2005): p. 32.

they have a higher VAT amount due to the large number of tourists.[19] Also the fourth source replaced the VAT source as filling up measurement. With the next decisions in 1992 and 1999 the quota related to the GNI will be reduced to 50% and the ceiling of the assessment base reduced in two steps to 0,5% by 2004.[20]

1.2.3 GNI based resource

The GNI based resource was introduced in 1988 with regard to the issue of equality as the argumentation is that the GNI reflects the economic strength and the ability to pay better than the VAT source. With the introduction of this source the overall budget was limited for the first time to 1.2% of the EU wide GNP. Also the compensation mechanism for the UK was modified that there is no change for them. Apart from minor changes like the slightly increased limit of 1.27% of the EU wide GNP, the next step was made with the Agenda 2000. From now on have the four biggest net-payers: Netherlands, Germany, Austria and Sweden only to pay 25% of the UK compensation amount, this amount in turn has to be paid by the remaining member states.[21] The GNI based resources has replaced the VAT based resource as filling up mechanism and become as the VAT resource before, the most important source of funding the EU budget from 1999 on, contributing today more than 70% of the income side in the budget.

1.3 Summary

The own resources system of the EU had become more and more complicated over the years. As long as the traditional own resources provided enough money there were no major discussions, supported by the fact that the revenues are not linked to specific member states. With the planned introduction of the VAT based resource the system gets more complicated, it took five years longer to implement it and another six year until the British rebate was added to the own resource decision officially. The years before special agreements were approved by the Council

[19] Cp. Euler, Markus (2005): p. 35.
[20] Cp. Raddatz, Guido (2005): Das Eigenmittelsystem der Europäischen Union, p. 41.
[21] Cp. ibid: p. 42.

on a yearly basis, concerning the net-deficit of the UK. The assessment base of the VAT resource is already a highly complicated mathematical system that is hard to understand without special knowledge. With the introduction of the UK rebate the situation get even worse. During the last own resources decisions more and more exemptions were established though the backdoor, as the increased reimbursement rate for the traditional own resources and the compensations mechanism for the biggest net-payers concerning the compensation amount of the UK. Summarised efforts made over the years to reach an equally, transparent and rational system as the introduction of the GNI based resource, the current state of the own resources system is not equal, neither rational, nor transparent as certain member states gets directly or indirectly discounts complicating all.

2. Analysis of the own resources system

In the following chapter the EU budget system will be regarded in detail. As the EU is an organisation "sui generis" it will be interesting what the EU budget has to fulfil compared with other international organisations and national states. Therefore it will be first analysed what the budget functions are and how they are implemented on the European level. For this the theoretical background of the allocation, distribution and stabilisation triangle designed by Musgrave[22] in combination with the fiscal federalism theory by Oates[23] will be used, to see how a rational finance system could work from an economical perspective.

Second the question about how to finance an institution like the EU will be raised in conjunction with the distribution of power on the different levels and possible changes.

Third the decision making process will be examined on the different stages and different institutions participating.

Afterwards a set of criteria concerning budget principles will be used to see if there are weak points of the current budget constitution.

Analysing these different points should make it easier to categorise the current system as well as possible inferences for reform approaches.

2.1 Budget functions

The structure of the EU is complicated, as it is neither a federal state system, nor a confederation. This affects also the financial system of the EU, because there is no example organisation.[24] Instead, the EU is a quasi federal system with a supranational identity to be situated between the two states mentioned before. The theory of fiscal federalism might not be applied completely on the EU, but most of it can be used to identify possible structural problems within the financial system of the EU.

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[22] Musgrave, Richard : US-economist
[23] Oates, Wallace E. : US-economist
[24] Cp. Euler, Markus (2005): p.110.

2.1.1 Allocation

Traditionally the fiscal federalism theory analyses the allocative efficient function and expenses policy, as well as the corresponding needed income competency of the different state levels.[25]

Public goods which have an EU wide effect should be allocated by the EU. This could be trans-European traffic networks, energy and communication networks. This applies also to public goods with a border crossing spill-over such as the use of rivers. Another point are economies of scale, this means public goods can be allocated more cost efficient if they are transferred to the most centralised level.[26]

All other goods should be allocated decentralised as smaller units can react better on individual demands. This aligns with the subsidiary principle of the EU treaty.

2.1.2 Distribution

Distribution in conjunction with the EU can be classified into two categories, distributions among member states and second on the citizen level.

Distribution among member states on the base of cohesion policy is useful to reduce regional disparities.

On the level of individual citizens distribution must be regarded from another perspective. In contrast to the national state level, mobility of labour force within is still limited and consequently redistribution is not ultimate needed. Another problem is the lack of a common base for such redistribution, as social policies are not harmonised and the discrepancy between individual member states is high.[27] For the future this could be from a bigger significance as mobility tends to rise.

2.1.3 Stabilisation

Stabilisation policies should be located centrally. As the monetary policies are located on the supranational level at the ECB the fiscal policies remain on the na-

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[25] Raddatz, Guido (2005): p. 76.
[26] Cp. Wegener, Sybille (2003): Fiskalischer Föderalismus. Theoretische Grundlagen und Studie Ungarns, p. 59.
[27] Ibid : p. 60.

tional levels.[28] Upcoming problems must be differentiated. There can be macroeconomic problems as a general lack of demand. In such cases the EU should grab the initiative and launch demand stabilising programs.[29] If there are structural problems, these can be better solved on the national level as the problem is more specific. Another problem is the uneven situation of economic growth within the EU that makes it nearly impossible that every national state can profit from a measurement on the supranational level.[30] Apart from the discussion if measurements are reasonable or not the main problem are the funds available for disposition. The volume of the EU budget compared to the budgets of the member states is really small, so it is questionable if measurements would have a significant outcome. This is complicated by the fact that the budget must be balanced and most of the money can not be transferred between different budget categories.

2.2 Options for financing the budget

There are two major options for financing the budget of international organisations. On the one hand you have contributions systems were money is funded from one jurisdiction to another and on the other hand you have own resources were the jurisdiction has an autonomous revenue raising power.

2.2.1 Contribution systems

Within international organisations[31], contribution systems are widely common. Significant for these systems are that the individual members decide on the funding, so in general there is an upward funding as the power to taxation remains at the lower level. Criteria for funding can differ; these can be that every member pays the same, that the contribution is linked to the GNI or on any other useful indicator. According to the agreement every member is independent in the acquisition of the contributions. These systems are often simple, spending orientated and

[28] Raddatz, Guido (2005): p. 95.
[29] Cp. Wegener, Sybille (2003): p. 60.
[30] Cp. Raddatz, Guido (2005): p. 98.
[31] Classic characteristics for an international organisation are: based on international law, established for long run and at least one body who articulate the common interest

have the goal to finance the organisation as long as there are no or not enough own resources.[32] Contribution systems do also work in the opposite direction when revenues are funded downwards; this is often the case when the most powerful jurisdiction is on the highest levels, as you have it in centralised nation states.

2.2.2 Own resources systems

In contrast own resources are revenues which are in amount an character entitles for the supranational level, independently from the will or a yearly decision in a national parliament. Own resource systems are clearly revenue orientated so spending is more dependent on the revenue side and do not afford the same level of planning security as contribution systems. Considering an international organisation as supranational the following criteria can be used as indicator: majority decisions are mandatory for member states, organs as a court are independent from the member states and the organisation should have financial autonomy. These systems are rather uncommon as preconditions for real own resources are the transmission of legal and revenue authorisation to the supranational level which would tangent a core principle of sovereignty.

2.3 Decision making process

With the agreement on a financial perspective the European Council of heads of state and government creates a multi annual framework for the EU budget. This states the general spending over a seven year period. In addition to that the Council votes unanimously on an own resources decision and such one remains valid until a new one is passed.

As proved many times before one single national interest can put the process into a deadlock. The increased number of 25 member states, 27 from the 1st of January 2007 means that for every small change in the own resources a new Council decision is needed.

The yearly budgetary process involves the proposition from the Commission which is send to the Council, in the next step modified by the Council. The EP can

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[32] Cp. Euler, Markus (2005): p. 106.

propose further details depending if spending is in an obligatory category or not. Then the proposal goes back to the Council with the possibility of accepting the changes made by the parliament or not. In the latter case the parliament can request a completely new proposal, but only when it is rejected by a two-third majority.

The balance of power shows that the member states are involved directly in all stages of the budget process through the European Council and the Council. This means they do not only decide on the amount of revenues transferred to the EU, they even have a major influence on the yearly budget plan based on the current share of power.

2.4 Budget principles

There are a range of budget principles that should be regarded during the budget process. In the following several principles were chosen to elaborate the issues of rationality, transparency and equality mentioned in the research question. This set of criteria will be used to analyse the current situation and to propose possible reform options. These criteria are from different categories consisting economical, political, technical factors and the level of integration.[33]

2.4.1 Transparency

Transparency should be given thus citizens who pay taxes should understand how the money is collected and spent. Therefore the only clear visible link are the traditional own resources as their imposition is related to EU legislation, but already here you can raise the question why member states can retain 25% of the duties, because that exceeds the real existing costs.[34]

The assessment base of the VAT resource has got more and more complicated over the years. Not only the general calculation established on theoretical harmonised index is complex, with the introduction of the UK rebate it is for ordinary citizens and even for interested people nearly impossible to follow the calcula-

[33] Cp. Euler, Markus (2005): p. 116.
[34] Cp. Raddatz, Guido (2005): p. 153.

tion.[35] In the following the introduction of the GNP resources the shift of the UK rebate in the latter category and the introduction of the de-facto "re-rebates" for the net payers leads to the conclusion that the member states with their own resource decision do not care about comprehensibility and transparency.

2.4.2 Financial autonomy

Fiscal autonomy allows space for implementing political goals. In the EU the spending is limited to the ceiling of the own resources decision. This decision is pending on the unanimously vote in the Council were national interests are normally the strongest ones within the EU institutions.[36] With a rising significance of the VAT and GNI resources that are de facto transfer payment of the member states, the net payer mentality and the rebate discussion gets more important. The common goals of EU policies become marginal; as not only the income side is restricted also spending in the traditional agricultural sector is a constant amount that has experienced several changes but still accounts for a significant part of the expenditure.

Fiscal autonomy on the EU level is quite low as member states have agreed to transfer competencies to the supranational level, but no fiscal competencies. So they hold their influence through the Council as institution regarded to the intergouvermental level.

2.4.3 Equity

Equity is hard to measure as it depends on the definition and the point of view. In general it is seen that equity should be linked with the ability to pay. This in turn implies that there are member states which pay more than they receive and is in contrast to the net-payer mentality were the principle seems to be you get what you pay for. The GNI resource is by far the most important, so equity is archived to

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[35] Cp. N.N. (2004): Financing the European Union. Commission report on the operation of the own resources system, p. 12.
[36] Euler, Markus (2005): p. 143.

a certain level. The major exemption is the UK rebate and the follow up rebates that have distorting effects on it.[37]

2.4.4 Equivalent principle

According to the fiscal equivalent principle every jurisdiction should obtain enough money to finance the tasks allocated. If this is not given by income from tax and other duties, finance transfers from another level within the system is the best way to solve the problem. In the case of the EU, the VAT and the GNI based resources can be grouped as finance transfers from another level, as the EU does not have the levy competence. Also important is the yield competence of the revenues, within the budget process the Commission adopts a proposal and the Council in conjunction with the EP decide on it. Even when the national member states decided to give competencies to allocate and distribute public goods to the EU level, they retain certain influence through to the Council.

Revenues that are not proportional allocated should be directed to the EU, as there are e.g. the custom duties. For the distribution competencies, the EU should be equipped with enough money to fulfil the tasks. Concerning the stabilisation it is obvious that the current budget is far too small to react on possible economic disruptions.[38] From that economic point of view the EU budget is capable to fulfil the tasks in general, but with the ongoing integration process the question will be if the current system is still working.

2.5 Implementation on the EU level

As already mentioned the EU is an organisation without any comparable institution. Also the budget of the EU is funded mostly by the so called own resources you have to look more precisely on that, as the criteria mentioned above do not apply fully to the EU own resources.

[37] N.N. (2004): p.15.
[38] Cp. Wegener, Sybille (2003): p. 62.

Without any doubt it is clear that the custom and agricultural duties are own resources, the member states are collecting them. Then they will be transferred to the EU apart from the expense compensation.

The VAT and GNI based own resources are harder to classify. The VAT revenue is calculated on the assessment base, but member states do not have to pay the amount directly from VAT revenues, they are free to decide where the money will be taken from. Even clearer is the GNI resource as the strength of a national economy does not produce a special tax where the amount will be deducted from.

The EU budget must be balanced which entails that the GNI based resource has a top level financing function turning the budget into a spending orientated one and this is a typically symbol of the contribution scheme.

Concerning the financial autonomy the EU is not dependent on a yearly new approved new decision of the member states, but every change within the own resources needs a new EU decision approved unanimously and that in conjunction with the binding rule of a balanced budget limits the fiscal autonomy.

Summarised the EU own resources system can not be entirely classified as such one, as there are too many points linked to a classic contribution scheme and the biggest part of the budget are the VAT and the GNI based resources. These are according to article 269 ECT own resources as they had been approved unanimously by the Council and ratified by the member states[39], but to classify them as own resources is only possible from a political perspective not from an economical one.

2.6 Sub-conclusion

The EC treaty simply states: "*Without prejudice to other revenue, the budget shall be financed wholly from own resources.*"[40]

Taking all the different aspects into account the current own resources system of the EU budget is not working properly nor fulfilling the requirements for a real own resources system.

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[39] Cp. Euler, Markus (2005): p. 115.

[40] Article 269, EC treaty.

First you have to state that apart from all problems the budget has adequate funding resources, the possible ceiling has not been reached during the last years and for the upcoming years the perspective is far below.

In contrast the balanced budget rule and the prohibition of credits limits the spending to the proposed revenue and this can result in projects not realised although there might be a political consensus before.

Regarding the budget functions and the funding a political discussion on the European level is needed to answer what level of integration is wanted for the future. Economists are discussing already the problem of stabilisation thus the monetary policy for the Euro-zone is transferred to the ECB whereas the fiscal policy remains on the national level. Indisputable such a transfer is only possible with a far more enlarged budget.[41]

Concerning the budget criteria the EU budget is in poor condition. With the latest financial perspective it becomes even more complicated, it is not transparent, not equal and has a very limited financial autonomy which is aggravated by the Council as powerful institution when deciding on the spending.

Summarised the budget has not become in any point more rational than it was during the last financial perspective. Reform options on most decisions within the EU must be agreed on unanimously therefore a radical change seems impossible in the short run, but the proposed evaluation in 2008/2009 shows that even the politicians are not satisfied wit the current system. In the following two different reform options will be discussed, the first one proposing changes within the existing system, the second one discussing options of an independent own resources system allocated on the supranational level.

[41] Euler, Markus (2005): p.133.

3. The new financial perspective 2007 – 2013

In December 2005 the EU summit reached an agreement for a new financial perspective for the EU. It is the first financial agreement since the accession of the ten new member states so the proposal is reflecting the interests of twenty five nations. With the ongoing discussion process since years it is interesting what reform steps are implemented with the new multi annual framework and if there are significant chances making the own resources system.

As known spending is limited to the revenues of the own resources, therefore it will be interesting to see how spending categories developed in the new financial perspective between the original Commission proposal and the finally approved version by the parliament.

3.1 The income sources of the new proposal

The own resources system will explore some minor changes. The assessment base for the VAT resource will decline to 0.3% in general. There are special agreements for Austria (0.225%), Germany (0.15%), the Netherlands and Sweden (0.1%).[42] This will have further effects on the GNI resource, thus missing incomes will be balanced there. Concerning the UK rebate there are modifications. The calculation of the rebate is percentage based, so the growing budget of the enlarged EU will lead to a bigger rebate in absolute numbers. Excluding the spending in the agricultural sector the part of the rebate caused by the ten new member states will decline by 20% in 2009, 70% in 2010 and from 2011 completely abolished. Effectively this measure will only slow down the development, in absolute numbers the rebate will grow. The difference between the old and the new calculation may not exceed 10.5 billion Euros for the whole seven year period.[43] Further exemption is made for Sweden and the Netherlands, their yearly contribution will be reduced by a fixed amount of 120 million Euros (Sweden) and 605 million Euros (Netherlands) respec-

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[42] Cp. Seiler, Hans-Werner (2006) : Die finanzielle Vorausschau 2007-2013 : Grundlage für eine handlungsfähige EU ? p. 179.
[43] Ibid: p.178.

tively. All in all the number of exemptions will explore a further increase among retention of the complicated own resources system.

3.2 The spending in the new proposal

The expenditure side of the EU budget has to regard the income side because of the balanced budget criteria. The EU has defined policy goals e.g. the Lisbon strategy, therefore it is interesting to see whether the money continue to flow into the agricultural sector which is highly criticised by non-affected politicians and a broad majority in the scientific literature or if spending becomes more innovative.

Table 1: Proportion of spending

	2005	2007 – 2013
Agriculture	43,2%	43,0%
Structural and Cohesion Funds	36,6%	35,7%

Source: EU-Budget 2005, Seiler, Hans-Werner (2006): p. 176.

Comparing only the two biggest budget categories there will be no significant change, despite from new category names[44]. Structural and cohesion funds are now part of the biggest category sustainable growth, but the subcategory competitiveness for growth and employment is far smaller than the already existing funds. Also the subcategories of the agricultural category, direct payments and rural development, remain stable. The accession of the new member states changed the average income per capita significantly. As only regions with less than 75% of the average income per capita are eligible to get money from the cohesion fund, as result many "poor" regions of old member states would loose funding. Apart from generous adjustment times for the affected regions up to 2013 many exemptions

[44] Heinemann, Friedrich (2005) : Der EU-Haushalt bis 2013 : Steigende Last, geringer Mehrwert, p. 59.

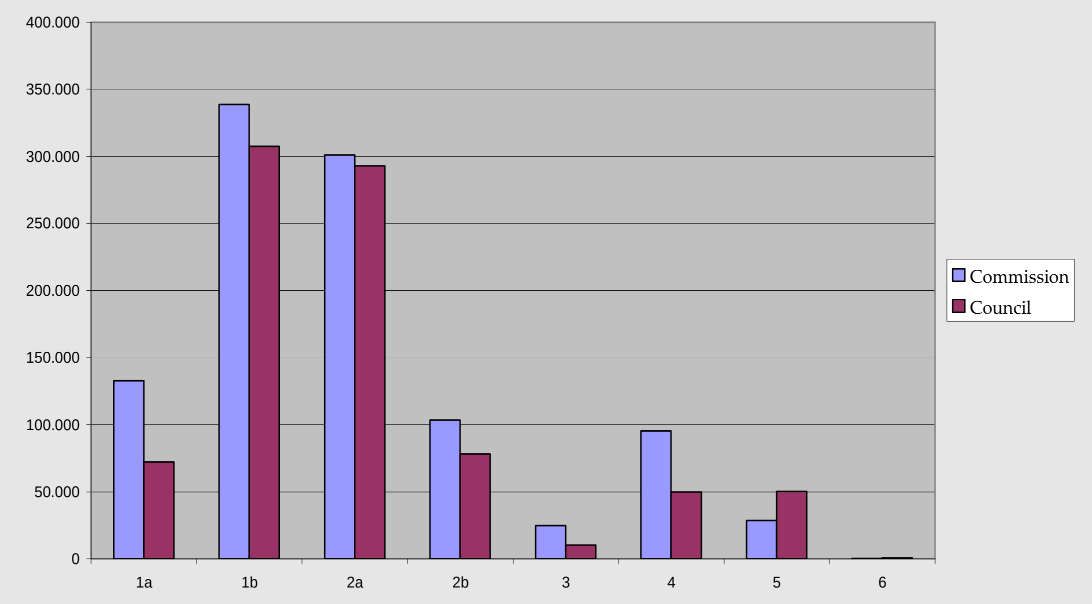
have been made. The list is incredible long consisting money for e.g. the Spanish exclaves in northern Africa, the east-German countries, Bavaria and Corsica.[45] It is not easy to find a logical explanation for all these exemptions, but as the structural and cohesion funds are the biggest category where the money gets back to the member states (agricultural payment got directly to farmers) it seems that the EU budget is not only limited by the net-payer mentality on the revenue side, but also by a take what you can get mentality on the spending side of the budget, not focussed on commonly agreed goals.

3.3 Commission proposal – Council proposal – Parliament

The own resources system are not only dependent on the actual own resources decision the decision process is also influenced by different actors. Therefore the changes between the Commission proposal and the final approved version by the Council and the EP will be analysed.

[45] Seiler, Hans-Werner (2006): p. 177.

Figure 2: Financial perspective 2007 - 2013



Source: Becker, Peter (2006): p. 108.[46]

The Commission proposal had a volume of 1.025 billion Euros, the final accepted version of 864 billion Euros. The table shows clearly that the categories targeting supranational aspects are these ones which had suffered the most loss. Especially category 1b, financing the goals of the Lisbon strategy, category three and four covering the second and third pillar of the EU. With the re-launch of the Lisbon strategy and the focus on growth and employment earlier in 2005 you would think that such a prioritisation has influence on budget decisions, but with round about 60% of the proposed Commission amount it does not reflect it.[47] Instead of this, the agricultural, cohesion and structural funds had only to handle cuts less than 20%. It seems that national interests were dominant at all stages of the discussion, cutting the overall budget to 1.045% of the EU wide GNPs and in saving the

[46] Categories: 1a: Competitiveness for growth and employment ; 1b : Cohesion for growth and employment ; 2a : CAP ; 2b : Rural development ; 3 : Citizenship, freedom, security and justice ; 4 : EU as a global player ; 5 : Administration ; 6 : Compensation

[47] Begg, Ian (2005) : Kohäsionspolitik und Lissabon-Strategie im EU-Haushalt - Konflikte und Vereinbarkeit, p. 697.

important budget categories, were money flows directly back to the member states or even better to the farmers.

The deal reached in December 2005 in the Council effectively cut the Commission proposal by round about 16%. The EP wanted an increase of twelve million for several projects. Finally they reached an increase of four million, two million directly spent the other two million are stored outside the expenditure side of the budget.

Table 2: Final agreement financial perspective[48]

	Commission	Council	Parliament
Competitiveness for growth and e.	132.8 billion	72.1 billion	+ 2.1 billion
Citizenship	24.7 billion	10.3 billion	+ 0.5 billion
EU as a global player	95.4 billion	50.0 billion	+ 1.0 billion

Source: EU press release

The numbers show that the parliament has a very limited influence, they reached one third of the amount of additional spending originally wanted. The final compromise may fund a few programs more, but comparing the Commission proposal with the final outcome it is obviously that the Council is the most important player during the negotiations over a new financial perspective.

3.4 Sub-conclusion

Summarising the developments of the new financial perspective you have to state that the results are disappointing. Apart from minor changes at the UK rebate the

[48] Numbers shown for the parliament are the overall increase of spending, only half appears on the expenditure side of the financial perspective

own resources system becomes even more complicated, as the VAT rates will be different for several countries and further indirect rebates for the big net-payer will be introduced. So the system does not get more transparent, equal or rational in any way. Even severe to see is that the Council cuts spending in categories necessary to implement the Lisbon goals and the parliament is not strong enough to oppose such movements more strongly.

4. Reform options within the current system

Politics on the EU level is in many cases a policy of small steps. The previous analysis implies that the whole system is not working properly if only rational and economic criteria were taken into account, but you have also to include the political reality. Therefore this chapter contains "small-step" solutions for the current own resources system. Besides possible changes concerning the calculation of the resources, there will be no shift in competencies between the participating institutions that would lead to an easier decision making process, thus possible changes in the voting system will be part of the propositions.

The traditional own resources contribute less than 12% to the EU budget and will probably explore a further decrease. This is related to the liberalisation tendencies on the world market.[49] It is widely accepted that this revenues should be allocated directly to the EU level the only critical point is the reimbursement for the collecting member state. The amount of 25% is far more than the real accrued costs. Thus the reform options are very limited to a possible lower reimbursement level to make this more rational, because of the general less importance of this resources there will be no further discussion.

The main focus is on the one hand the VAT based resource and on the other hand the UK rebate as well as the directly linked rebates for further member states.

4.1 VAT based resource

The VAT resource was introduced as filling up resource to finance the remaining part of the budget not covered by the traditional own resources. The main criticisms concern the calculation. Nearly all member states have more than one VAT rate, usually a full rate and a discounted rate. This already needs a harmonisation for the assessment base.

Following that the calculation is a multiple step process. First for every member state the assessment base is calculated with the respective limit to 50% of the GNI.

[49] Cp. Euler, Markus (2005): p. 165.

Normally the next step would be to price the amount of money to be paid with the current contribution rate. At this point the UK rebate complicates the system. The amount of money reimbursed to the UK (67% of the net payments) will be deducted from the UK part of the VAT resource. The money reimbursed has to be paid additionally by the other member states based on their GNI force, according to the valid own resource decisions, currently with further rebates for the four biggest net-payer.

Thus the maximum contribution rate can not be exceeded; a formula is used to calculate a virtual level below the contribution rate. To this lower rate the compensation amount of the UK rebate is added, so most countries effectively pay the maximum rate, if the amount exceeds the maximum rate the remaining money has to be paid via the GNI resource.[50] With the new decision there are various rates for the member states. The regular contribution rate will be maximum 0.3% of the assessment base, less for the biggest net payers. This means a further complication of the formula to calculate the virtual contribution rate, making the whole system of compensation amounts based on the GNI resource and then transferred to the VAT resource on of the most intransparent parts of the budget.

The proposed decrease of the maximum contribution rate from 0.5% to 0.3% for most states will lead under a practically stable assessment base to a decline of the VAT based resource amount of at least 40%. It is hard to estimate numbers exactly, but under such conditions the contribution of VAT resource to the budget will most probably fall under 10%. In addition to that a slightly growing UK rebate in absolute numbers will further reduce the virtual contribution rate.

At this point the question is, if the system of a VAT resource is useful in the future. The indicators needed for the contribution like the harmonised assessment base are only calculated for the VAT resource, they do not have any further economical relevance in contrast to the GNI numbers that are widely used. At the moment nearly half of the member states VAT contributions are cut because they would exceed the 50% of the GNI criteria. This leads de facto to a separated second GNI based contribution[51], raising the question what the significance of the resource

[50] Cp. Raddatz, Guido K. (2005): p. 188.
[51] Cp. N.N. (2004): p. 46.

is. The enlarged EU faces a bigger difference in terms of economic constitution of the individual member states, so their contributions to the budget will be most adequately based on their economical strength which is reflected in the GNI resource. Apart from the individual rebates that will be analysed in the following section, the most efficient way to make the own resources system more rational and transparent is to abolish the VAT resource, insert the lacking money into slightly higher contributions in the GNI resource. Such a step would lead to minimal changes of the individual member state contributions and a new debate about net-payments can be avoided at this reform option.

4.2 The individual rebates

The main point of discussion for years is the compensation mechanism of the EU budget. Firstly introduced in 1985 for the UK, but it is generally open to all member states having an excessive net-payment position that exceeds the benefits of EU politics. This does not imply that every net-paying member state has automatically the right for compensation, but if the cost-benefit relation is outside a certain limit it can apply for it.

4.2.1 Historical background and rationality of the UK rebate

The so called UK rebate was introduced formally with the own resources decision in 1985, but practically the UK received compensations since the accession in 1973. They were based on single decisions of the Council. The arguments in favour of a rebate of the UK government were the structural differences between the UK and the other member states, the agricultural sector has another type of peculiarity which resulted in less agricultural transfer than to the other member states and as well the general economic strength compared with the EU average. In the beginning the rebate seemed rational as indicators like the GNI of the UK and the share of expenses for the agricultural sector supported the British position. However over the years the indicators changed dramatically and the rebate still exists in the original version with small adjustments.

Table 3: Comparison of key indicators

	1984	2003
Share of expenses in the agricultural sector	73.0%	43.0%
British GNI per capita based on the EU-15 (EU-10) average	90.6%	111.2%

Source: N. N. (2004): p. 20.

The increase of the British GNI has two reasons, on the one hand the average of the EU GNI per capita explores some changes through the accession of Spain and Portugal in 1986 and on the other hand the British economy has been more prosperous than in many other member states during the last 20 years.[52]

Table 4: Estimated net contributions for the period 2008 – 2013

	Before correction	After correction
UK	- 0.62%	- 0.25%
Germany	- 0.52%	- 0.54%
France	- 0.27%	- 0.37%
Italy	- 0.29%	- 0.41%
Netherlands	- 0.55%	- 0.56%
Sweden	- 0.47%	- 0.50%

Source: N. N. (2004): p. 21 – 23.

The estimation of the EU Commission shows the expected net contribution of several member states during the next financial perspective. Not regarded is the final decision on the new financial perspective that includes the following changes. The UK rebate wills growth more slowly as non-agricultural expenditure will not reimbursed from 2009 on and the Netherlands and Sweden get a yearly extra discount. This results in slightly higher contributions of Germany and higher contributions by France and all other net-paying member states not eligible for the 75% rebate on the British compensation payments. Comparing the economical strength

[52] Cp. N. N. (2004) : p.20.

and the out of it derived ability to pay it is not rational why the UK as one of the most prosperous members still gets the big discount, why Sweden and the Netherlands stronger than Germany and Austria get the yearly extra discount and why countries like Italy practically on the same level as Germany are not entitles for the 75% discount on compensation payments.

Summarised the negotiations for the financial perspective do not betray any logical, rational decision concerning an equal system of contributions; instead it looks like a race for savings as much money as possible. Apart from that there is an ongoing discussion about rational possibilities to limit exceeding net-payments.

4.2.2 General compensation mechanisms

Since almost twenty years a revised compensation mechanism not only limited to the UK is discussed more or less frequently. In the late 1980ies it was the proposal of Padoa-Schioppa[53] containing a safeguard mechanism, in the 1990ies it was the proposal by thy finance ministers of the biggest net-payers proposing a generalised system close to the existing UK rebate. In 2004 the Commission published a proposal based on previous discussions offering a concept of a general compensation mechanism showing different ways of implementation.

A main component is a threshold, as it was already suggested in the proposal of the finance ministers. In a first step it must be defined which parts on the revenue and on the expenditure side of the budget are taken into account for the mechanism. On the revenue side it is clear that the traditional own resources are excluded, because they can not be located to a single member state. On the expenditure also nearly all categories are included except external policies, pre-accession spending and other minor categories.[54]

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[53] Italian economist, currently minister for economy and finance in the Italian government

[54] Cp. N.N. (2004): p. 29.

4.2.2.1 Threshold

According to the Commission there could be two different options for implementing a threshold, a fixed one or a variable one. A fixed threshold could range between 0.0% and – 0.5% of the national GNI net contribution.

Table 5: Corrections with a generalised mechanism (67% reimbursement)

Level of the threshold (% of GNI)	Sum of all corrections
-0.00%	25.8 billion
-0.10%	19.8 billion
-0.25%	11.1 billion
-0.40%	5.2 billion
-0.50%	1.9 billion

Source: N.N. (2004): p. 31

Realistically it would be anywhere between - 0.25% or above, thus a lower threshold would exceed the amount of the current mechanism. To include the ability to pay even more a variable threshold could be implemented. In that case the threshold could be linked to the GNI per capita in purchasing power parity. This would lead to faster contributions for countries with a general lower income and to lower contributions for the already above average countries.[55]

4.2.2.2 Ways to fund the correction

There are at least three ways of financing the upcoming correction. One possibility is to exclude all states receiving a correction from the payments. This would result that net-receiver countries would pay all of the correction. Another possibility is that all members pay the correction except their own. This would rather complicate the mechanism and ignoring the transparency criteria. The final possibility is that all member states finance the whole contribution based on their share of the GNI as it is already implemented in the GNI resource.[56]

[55] Cp. N.N. (2004): p. 33.
[56] Ibid: p. 35.

4.2.2.3 Final Steps

In a final step it should be discussed if there is only a single rate of reimbursement or preferring a declining rate based on the amount of money or the economic strength. Also a possible risk is exceeding corrections therefore a maximum amount should be included in the planning.[57]

4.3 The decision making process

One of the main problems of the EU budget is the separation between the revenue and the spending side. Whereas the spending is decided in the Council with a qualified majority and a majority of the parliament, the revenue side can only changed by a unanimously Council decision.

There are propositions to move the revenue process from the constitutional level to a policy level which would lead to qualified majority decisions. Recapitulating for a qualified majority decision are needed approximately 73% of the weighted votes in the Council[58], an absolute majority of member states and 62% of the population. As the three conditions allow a not to small minority to block a decision and Council decisions in parts were majority rule is already introduced remain most of the time unanimous, it seems unlikely that one of the two contrary positions in favour or against an enlarged budget could decide against the other party.

Another proposition is the introduction of voting by veto, a model developed by Dennis Mueller. Every member state has the right to introduce a proposal after that the current decision is added as an additional one. Then according to rules that need to be defined, every member state submitted a proposal has the right to veto one. Thus the system only works when every proposal gets one veto, member states must do that in a row. The remaining proposal will be the approved one.[59]

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[57] N.N. (2004): p. 33.

[58] See treaty of Nice for exact numbers

[59] Blankart, Charles B. and Christian Kirchner (2003): The Deadlock of the EU Budget an Economic Analysis of Ways In and Ways Out, p. 27.

Concerning the competencies between the Council and the EP it could be a useful proposition to give the parliament also the last-deciding right on obligatory spending as it already has for non-obligatory spending.[60] This would include also the agricultural funds a change could possibly achieve more easily in the Parliament than in the Council. Every decrease taken on the big spending categories side of the budget would result in a lower pressure for a reform of the own resources system, as the categories on the supranational level should profit from more available money.

4.4 Sub-Conclusion

There are various starting points for reforming the current own resources system internally. As already stated the VAT resource are on the one hand incredibly complex, on the other hand dispensable as there is no economic significance between the current collection of the VAT source and the GNI source. Abolition would not harm any member state severe, but perhaps it is the then following reallocation of the rebate and an upcoming discussion that prevents the member states form that at the moment. This would already bring much more transparency to the own resources system, but it would rather change nothing in the current inequalities.

Therefore a reform of the UK rebate is necessary. A new compensation system might be not economic justifiable, but it is rather unlikely that the net-paying mentality will disappear from one day to another. Therefore a negotiable decision based on the Commission guidelines would lead to more equity and making the own resources system more rational. As most of the member states would profit from such compensation except the UK[61] it is questionable if a reform is possible without redistribution between the different expenditure categories.

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[60] Lippert Barbara and Wolfgang Bode (2001): Die Erweiterung und das EU-Budget - Reformoptionen und ihre politische Durchsetzbarkeit, p. 379.
[61] Cp. Euler, Markus (2005): p. 215.

The propositions concerning the decision making process are rather improbable as they need a broad consensus or in the case of voting by veto are simply theoretical remarks within the scientific discourse.

5. Reform options outside of the current system

This chapter will contain proposals changing the current own resources system. The main focus will be the ongoing discussion about a shift of taxation to the EU level. In contrast to the preceding chapter all steps would require more reform will; therefore the realisation of the concepts will be taken into account. To evaluate if a taxation would be more rational, the already introduced budget criteria can be used and a few other factors.

5.1 Requirements for an EU – tax

The concept of an EU tax appeared already several times, but mostly facing strong resistance from several member states including the UK, because a substantial change of the own resources system always endangers the rebate. Surprisingly Prime Minister Blair announced at the end of the British presidency that the EU has to search for the best way to fund the budget, stating that this could include an EU tax.[62] Even with a growing support the advantages of an EU tax must be enormous before the national states transfer the power to tax, in a very limited way to the EU. In the following the most important factors will be named.

5.1.1 Sufficiency and stability

One of the most important factors is sufficiency. The EU must first decide how a new own resources system should be designed. A possible EU tax could be replace one of the existing resources but it has to be clear if it is the filling up resource of if there are still contributions as filling up resource. Additionally the resource should be extendable if new working fields come to the EU competency.[63]

An EU-tax should be stable and predictable. As taxes tend to fluctuate only such ones remaining relatively stable, as much independent form the economic cycle could be a useful alternative to the contribution system. Otherwise it seems only possible when the balanced budget rule will be abolished.

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[62] Crolly, Hannelore (2005) : Blair denkt über EU-Steuer nach

[63] Cp. Cattoir, Philippe (2004): Tax-based EU own resources: An assessment, p. 8.

5.1.2 *Efficiency and transparency*

A new EU tax should transparent. In nearly all cases a newly introduced tax would be clear visible thus the tax is deducted at any place separately, instead of the contributions of the member states that can be paid, from tax revenues not specified of the national budget.

Such a tax should have low operating costs. This means it will be useful to collect taxes at a point where they are already collected as a supplement or were they are easy collectable. Complicated assessment bases should be avoided.[64]

5.1.3 *Equity*

A new EU tax should provide equality in different ways. On the one hand it is interesting whether the tax will have equal impacts on the tax payers and on the other hand the tax should be linked to the economic level of the member states and the ability to pay.[65]

5.1.4 *System*

There are at least three different systems for collecting taxes in a federal system. The first one is the network system. In such a system different governmental bodies are sharing revenues from a collected tax. In this case it would be the EU and the national governmental level. As tax harmonisation is a difficult task, it is nearly impossible to reach a commitment within a network system and without a harmonised assessment base in the national states it does not make much sense.[66]

The second option is add up system. Here you have the two different bodies collecting separately from the same assessment base the same tax, but every body as an individual contribution rate. This system could be a possible option for the EU as the citizen get a clear image what he has to pay to the EU, also it could be easily collected as the member states doing it already. A main problem remains, the assessment base must be harmonised to archive a certain level of equity.

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[64] Cp. Cattoir, Philippe (2004): Tax-based EU own resources: An assessment, p. 10.
[65] Cp. Ibid: p.12.
[66] Cp. Raddatz Guido and Gerhard Schick (2003): Wege zur europäischen Verfassung – Braucht Europa eine Steuer? P. 8.

The last system is a separated system. The EU and the member states agree on a separation of taxation, so any kind of tax could transferred to the EU. The EU in turn would then have the right to determine the assessment base; no harmonisation on the national level is needed.[67] Such a big step is seen critical by several member states thus a tax relocated at the EU is the power to tax is not longer in their control, whereas a tax in a network system is part of negotiations when a change occur.

5.2 Possible EU-taxes

The Commission proposal outlines three different options for an EU tax. This includes an energy-based fiscal resource, a real VAT based fiscal resource or a fiscal resource based on corporal incomes. In the following the options will be analysed with the criteria stated above and if such s option is politically feasible.

5.2.1 Energy based fiscal resource

The introduction of an energy based fiscal resource can be implemented in different ways. Many competencies in the energy sector are under the organisation of the EU as the liberalisation of the energy markets or the European traffic route network, so there would be incorporation to energy based tax. Proposals range from a tax on all energy sources to more specific suggestion about a tax on traffic fuels or CO^2 emissions.[68] The Commission proposes a fiscal tax on motor fuel and on air traffic. The difference between the two sections is big, thus on motor fuel the EU already agreed on a minimum harmonised taxation whereas air traffic especially kerosene is still exempted from tax deduction.[69]

Sustainability and stability can be reached with the proposal. Taxes on motor fuel are quite stable the consumption declines slightly in the richer countries due to technical improvements but overall it remains very stable and predictable. Parts of the already harmonised minimum taxation could finance large parts of the budget

[67] Cp. Raddatz Guido and Gerhard Schick (2003): p. 11.
[68] Cp. Cattoir, Philippe (2004): p. 20.
[69] Cp. N.N. (2004): p. 59.

if they will transferred to the EU level, according to the political decision about the whole own resources system. It is hard to predict the revenue from an aviation or CO^2 tax as there is no experience with it and due to international regulations concerning the air traffic problems could arise concerning the international sector outside of the EU.

Efficient solutions easy to reach for the taxation of fuel, part of the revenues have to be transferred to the EU, this could be the same way as before in an add up systems. Transparency is a minor problem as citizens show a high sensibility when energy taxes are changing.

The equity criteria is fulfilled for a fuel tax as every citizen pays the same tax rate at every place in the EU, additionally he will pay the national tax and these ones can differ between the countries. The national countries all transfer an equal amount per consumption and retain the additional taxes based on economical strength or their environmental policy.[70] A possible CO^2 emission tax in contrast would not be so equal, as European countries with less economical strength still face older factories and a higher emission than countries with strong ecological 2standards.

5.2.2 VAT fiscal resource

The intention of the VAT fiscal resource is to crate a direct link between the EU and the citizens. The proposal sets a rate of 1% for the resource. At a possible introduction time the national VAT rate should decline by 1%, so expenditure neutral for the citizens. This add up system exists already in the USA were the states add up their VAT rate to the national VAT rate. In case of the EU it would be the reverse way, as the EU rate would reduce the national VAT rate by this amount. A step stone are the goods liberated from the VAT, because the range of them differ between the countries.

The criteria of sufficiency and stability are given. The assessment base of the EU wide VAT is more than 4.000 billion Euros, the proposed 1% rate would lead to 40 billion Euros for the budget. For the next financial perspective such a resource

[70] Cp. Cattoir, Philippe (2004): p. 23.

would fund 33% of the budget. Whenever a decision is needed to raise the tax, minimal changes do have a big impact on the revenue side. VAT is one of the most stable tax resources it is relatively predictable and therefore useful as a possible tax based own resource.[71]

The tax can be efficient, thus it is already collected by the member states so the existing systems can be used and an agreement rules the transfer process to the EU. The add up system is the most likely for this proposal. Transparency for the citizens will be also increased as a separated VAT tax for the EU could be displayed individually with every purchase.

The situation will be different when it comes to the equity principle. The standard rate is proposed at 1% for every member state, so there will be no differentiation between poorer and richer countries but in general it reflects the ability to pay for the governments thus 1% revenue in poorer countries will be lower than 1% in richer countries not dependent on the overall VAT rate. The individual citizens will according to the proposal not face more or less costs but people of a low income group spend proportionally more on the VAT than high income groups.[72]

5.2.3 Corporate income fiscal resource

The last Commission proposal is a tax on corporate incomes. There have been no big harmonisation efforts in this sector. This results at the moment in 25, respectively 27 different national member states systems. A commonly consolidated tax base would be the first step making such a tax possible.[73] Thus an EU wide corporate tax would require a complete re-structure of the taxation including the imposition on EU level there is big opposition from the national member states, even it remains possible to add a national tax rate.

Sufficiency can reached with a certain tax rate. The main problem is the fluctuation of corporate taxes in conjunction with the economic cycle. If this tax is used as

[71] Cp. Euler, Markus (2005) : p. 256.
[72] Cp. Ibid : p. 257
[73] Cp. Cattoir, Philippe (2004): p. 17.

a major income source for the budget it could be problematic to compensate yearly fluctuations, so stability is not totally given.

If such a tax can be organised in efficient ways is questionable, as harmonisation is complicated thus member states systems vary from flat tax systems to progressive tax systems. Transparency is a minor problem, citizens can see what tax is used to finance the budget, but perhaps the interest is lower as the vast majority of citizens would not be directly affected.

Equality for the individual citizen is hard to measure because he is not paying the taxes, but certainly any kind of allocation and redistribution on the national level is done. It is even harder to estimate the effects for the member states as there is no common assessment base, but revenues from corporate taxes varying between 1% in Slovenia and 7.8% in Luxemburg according to the national GNI.[74]

5.3 Comparing the different tax propositions

Table 6: Comparing analysis of different tax options[75]

	VAT tax	Environment tax	Corporate tax
Sufficiency and Stability	+	+/0	-
Efficiency and Transparency	+	+/0	0
Equity	0	+/-	0

Source: own design

The analysis according to the criteria between the different options shows a preference towards a VAT based or environmental taxation on motor fuel. The clear advantage of both would be that there already had been harmonisation efforts and that a commonly consolidated assessment base is feasible. The revenue is

[74] Cp. N.N. (2004): p. 59.

[75] Environment tax: first indication related to a motor fuel tax / second indicator for a CO^2 emission tax

predicable and the whole assessment base is big enough to raise the tax if needed, so such a tax could finance big parts of the budget and provide the EU a higher level of fiscal autonomy. Collected in an add up system it would be transparent to the citizens. Both taxes would have a single rate that means they are not progressive, so all income groups pay the same linear amount based on consumption, therefore the equity criterion is only rated balanced. A CO^2 emission tax and the corporate tax have poorer ratings, as they are not easy to predict or in case of the corporate tax varying with the economic cycle. There is no experience with a CO^2 tax but it is likely that transparency is hard to achieve because of the complexity of the calculation, the corporate tax need a lot more harmonisation efforts to be efficient. Concerning equity the CO^2 tax burdens economic weaker countries as they have lower environmental standards, a corporate tax have to be faced by all corporate tax payers, but it is likely that the national tax addition would vary widely.

5.4 Feasibility of an EU wide tax

Based on the previous examinations about transparency and rationality of an EU tax, the next step is the political feasibility. The main point here is the possible shift in the power of taxation. In the current system the member states decide on the revenue, whereas the Council and the EP decide on the spending. Many politicians of net-paying countries have fears that with a power shift the EU budget will increase significantly because of an expanded spending possible through a raise of an EU tax.[76]

According to Commission proposal the citizens should not pay more than before a possible reform. As the financial situation of most o the member states is quite bad it is likely that citizen’s pay effectively more and that in conjunction with the EU would not lead to better view of the citizens concerning the EU. In Germany VAT is shared between the national government and the states, contributions to the EU budget are paid from the national budget so a possible introduction of an EU tax concerns not only the national governments of the member states and this makes the process rather complex.

[76] Cp. Heinemann, Friedrich (2003): Braucht Brüssel eine eigene Steuer? P. 84.

Finally the question of rationality concerning the net-payer mentality would probably not change, thus an introduced EU tax would lead to more flexibility in regard to the expenditure. With the qualified majority mechanism in the Council it is likely that spending in the categories agriculture and structural funds will not fall under the current level as every member states wants as much money directly and visible back as possible.[77]

Summarised the introduction of an EU tax could be a major change to the current own resources system, but without a general re-direction of spending and commonly policy goals that receive a sufficient funding, it would be not successful in terms of a more rational budget. In contrast the transparency criteria will be achieved likely with an introduction of an EU tax, but this alone is not enough.

[77] Raddatz Guido and Gerhard Schick (2003): p. 12.

Conclusions

Facing the question how the EU own resources system can be reformed to reach a more transparent, equal and rational system of funding the EU budget is not easy, as institutional structures are more complicated than in other international organisations.

First you have to state that the own resources system is under continuing criticism from members of national governments, EU bodies or people with a scientific, economic background and the current system does not fulfil several requirements as transparency, efficiency and financial autonomy, so the system is not rational at the moment. The system has become more and more complicated over the years and the last introduced own resources decision approved in May 2006 does not change anything significantly.

Second, reform on the own resources does not automatically lead to an improved financial system, as spending must be regarded. As long as the budget must be balanced and there are fixed expenditure categories as the CAP, the overall spending remains rather limited.

Third, reforming the current own resources system, which is de facto overwhelmingly based on an upward funding will probably lead to more transparency concerning the assessment base of contributions, but not for the citizens. A proposed generalised rebate system will improve equality among the member states. But still it is questionable of such a reform of small steps will change significantly the situation and lead to more rationality. Another question is how long the EU will be capable to finance the tasks given by the member states with decreasing volume based on the EU wide GNP.

Forth, the introduction on an EU tax as proposed a VAT tax or environmental fuel tax are partly suitable as a new own resource. They would lead to bigger transparency and the own resources system would become more equal. But also here it is to mention that financial autonomy not automatically increase if nothing is changed on the spending side. Coming back to the budget functions and principles it is useful to allocate taxation of goods to the EU level that are not proportionally distributed.

Fifth, a reform of the institutional setting should be regarded. National governments try to save as much money as possible blocking major reform movements. The national governments decide over the own resources, they make the rules for compulsory spending and they interfere through the council on the budget planning, although it is concerning supranational issues were all other competencies have been transferred to the supranational level. As long as a reform of co-decision seems not possible, the role of the parliament should be enlarged, by lower majority requirements to disagree with the commission and the parliament should get the last decision right. In a final stage it would be good to have a system as in national states were revenue and expenditure were proposed from one institution and another one is deciding on it, instead of a competence clutter.

Other reform options to ease the financial situation could be the following. As national member states do always have on the one hand the fear of paying too much and trying to reduce contributions and on the other hand not willing to reform cost extensive uneconomic sections as the CAP, new finance systems could be discussed. One of them could be a new distribution between the EU and the national level. Without reducing the overall of money spent in sectors as the CAP the percentage paid by the EU can be reduced step by step, the remaining part would have then paid by the national governments. This would reduce contributions in general and increase the pressure on national governments.

Another proposition could be a split within the budget between categories with different characters. On the one side you will have the categories having a clear supranational character as spending in education and research activities on the other side you will have the classic categories as the CAP and the cohesion funds. The first one could be paid by real own resources where the EU has the power to taxation, whereas the latter one could be financed by a classic contribution scheme as not generally all member states gain the same profit from it.

Being realistic about the reform will of the EU, the next scheduled round of discussion in 2008 should focus on internal solutions. It is simple and clear the VAT based resource including the UK rebate should be abolished. With this step the budget would be far more equal than now. Member states are paying contributions among there ability to pay related to their GNI outcome. As radical decisions are quite unpopular a general correction mechanism according to the Commissions proposal could be introduced.

In general the EU should think about a general new adjustment of the fiscal resources based on economic principles as earlier proposed, but as long as the constitutional treaty is not ratified there seems no space for discussing this issue. So the current own resource system is still a working model for the EU, but not a good one.

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Annex

Data used for graphs

Figure 1:

Year	Agricultural duties	Custom duties	VAT based resource	GNI based resource	Miscellaneous
71	30,6%	25,0%	0,0%	0,0%	44,4%
73	10,4%	40,4%	0,0%	0,0%	49,2%
75	9,2%	49,3%	0,0%	0,0%	41,4%
77	20,5%	45,3%	0,0%	0,0%	34,2%
79	14,4%	34,8%	31,8%	0,0%	18,9%
81	9,2%	33,8%	48,6%	0,0%	8,4%
83	9,5%	28,1%	53,2%	0,0%	9,2%
85	7,8%	29,6%	54,2%	0,0%	8,4%
87	8,7%	25,0%	65,6%	0,0%	6,7%
89	5,2%	22,5%	57,3%	9,8%	5,2%
91	4,4%	20,4%	55,8%	13,3%	6,1%
93	2,9%	16,8%	52,5%	25,2%	2,6%
95	2,6%	16,7%	52,2%	18,9%	9,7%
97	2,4%	15,2%	42,5%	33,4%	6,5%
99	2,5%	13,5%	35,9%	43,2%	5,0%
01	2,1%	13,0%	35,6%	48,5%	0,8%
03	1,5%	11,0%	24,7%	60,9%	1,9%
05	1,5%	10,1%	14,4%	73,0%	1,0%

Figure 2:

	Commission	Council
1a	132.755	72.120
1b	338.710	307.619
2a	301.074	293.105
2b	103.581	78.140
3	24.705	10.270
4	95.350	50.010
5	28.620	50.300
6	240	800