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Center for Applied Policy Research

spotlight europe
2007/08 – November 2007

Europe's Finances - The old system at its limits

Wolfgang Schüssel
Leader of the Parliamentary Group of the Austrian People's Party (ÖVP)
Former Chancellor of the Austrian Republic, wolfgang.schuessel@oevpklub.at

The current system of EU revenues is opaque, complicated and unfair. That is the reason why it ought to be changed. The forthcoming budget review therefore offers the opportunity for a significant reform. The European Union needs greater financial flexibility in order to fulfil its global commitments. An EU tax should be considered, which would raise the level of the EU's own resources.

The negotiations devoted to the EU financial framework for 2007-2013 have demonstrated that the current EU financial system has reached its limits. On 10 September 2007 the European Commission launched a "no taboos" debate about the post-2014 budget structure. José Manuel Barroso, the President of the Commission, has emphasized that "everything will be discussed". If honest financial arrangements are what we really want, then the forthcoming review by the Commission will have to scrutinize all the various different issues - own resources, rebates, exceptions, and expenditure.

An important feature of the agreement on the financial perspective for 2007-2013 reached by the heads of state and government at the European Council in Brussels on 15 and 16 December 2005 was the revision clause, which stipulates that there will be a comprehensive review of the EU financial framework as early as 2008/2009.

This does not leave us with a great deal of time. In the coming months we need to conduct a debate about a comprehensive and qualitative reform of the EU budget, and this needs to be initiated now.

I

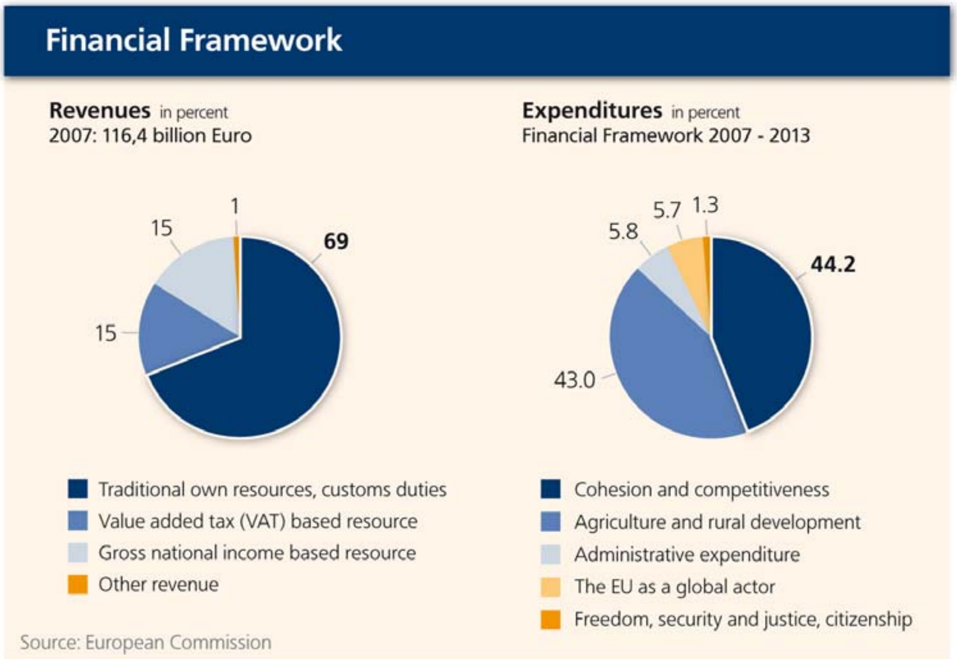
The old system

From 1958 to 1970 the Community budget was financed exclusively by contributions from the member states. In April 1970 the Council meeting in Luxembourg voted to introduce a system which envisaged revenues in the form of own resources to finance the Community budget.

Initially the only own resources were the customs and agricultural duties levied as a result of EU responsibility for the areas of agriculture and foreign trade. These were transferred directly to the EU. Since 1980 these revenues have been augmented by a percentage of VAT, which is calculated on the basis of a complicated formula that takes into account gross national income (GNI). Currently, to put it simply, it constitutes about 0.3 per cent of the VAT tax base.

Furthermore, there are also national budget subsidies, which are calculated on the basis of GNI, that is, the economic size of the individual member states. They include the "UK rebate", and, in the current financial perspective, rebates for other "net contributors" (Netherlands, Germany, Sweden, Austria).

The time is now ripe for reforms and changes. There is an urgent need to alter the present system. For this reason a resolution of the disagreements about the EU budget framework cannot be deferred until 2013, when the next financial perspective will be drawn up. During the negotiations of the European Council in 2005 the Commission was asked to carry out an analysis of all aspects of EU expenditure, including the Common Agricultural Policy and the UK budget rebate, and to present a report on this in 2008/2009. The European Council will be able to use this to make the urgently needed decisions, and at the same time will take into account the preparatory work for the next financial framework and the period after 2014.



However, differing interpretations of this issue began to emerge as early as 2005. The then French President Jacques Chirac described the budget review as being nothing more than a "fig leaf" designed to conceal the British budget concessions, and he sought to defer any kind of reform of the Common Agricultural Policy to the period after 2014. On the other hand, the British construed the 2008/2009 review as the basis for a substantial reform of the expenditure side of the budget before 2014.

The debate about the EU budget has resumed as a result of the European Commission's internet presentation of the EU's medium- and long-term expenditure priorities, which covers all aspects of the issue.

II

Commission prepares budget review

The Commission believes that the budget review constitutes a unique opportunity to include the numerous EU budget issues in a wide-ranging "no taboos" debate which can be conducted without the looming presence of negotiating pressure. It is unlikely, in the wake of all the topics that have been discussed, that the Commission will submit a proposal for the new 2014 budget framework before the autumn of 2009, by which time its membership will have changed.

The wide-ranging debate envisaged by the Commission will be preceded by a Common Agricultural Policy "health check". In addition to agricultural policy, it will be necessary to discuss the structural and cohesion policies and how they function within the framework of a European Union that now has 27 member states. The Fourth Cohesion Report published in May 2007 contains the material required for such a debate.

I think that the reforms which must subsequently be introduced should take their bearings from four salient points:

- The current system is opaque, complicated and unfair.

- The reforms relating to revenue and expenditure are interdependent.

- The discussion must include all of the rebates.

- An additional EU tax based on income or wages is out of the question.

Of course, the participants are all well aware of the fact that it is difficult to change a structure which has developed over the course of several decades. However, I do not think it is right that 90 per cent of EU budget revenue derives from the national budgets.

The EU is in urgent need of new own resources. As we have seen, 50 per cent used to come from customs duties. So we should think about those things which are currently not taxed at all and could in fact be used to generate own resources.

III

A "no taboos" debate

I suggested as early as 2005 (Süddeutsche Zeitung, 31.12.2005) that, if the reform debate fails to come up with a new budgetary mechanism, the governments will be "up in arms" by 2011 at the latest. For this reason, when presenting the programme of the Austrian EU Presidency to the European Parliament on 18 January 2006, I emphasized that the financial perspective is a particularly important subject for the Commission, the Council and the European Parliament:

"Greater self-financing is maybe not popular, but necessary."

"The financial perspective, which covers seven years, provides security and makes it possible to plan ahead. (...) I want to be clear: we will reach our limits if we keep imposing new tasks on our national budgets. If we carry on like this, the present financial perspective could be our last. I am now going to say something that not all of you will agree with: Europe needs more self-financing. We cannot continue to carve everything that we need for Europe out of the national budgets. It could end in that uncomfortable tension between net payers and net recipients. Greater self-financing is maybe not popular, but necessary. The President of the Commission, Mr. Barroso, also takes a similar view. The Commission must put all of these aspects on the table in its 2008/2009 review. We cannot have a situation where short-term financial speculation is entirely exempt from taxation, or where air or ship transport are entirely exempt from taxation. I would ask the Commission to include these topics in its review. I would also ask the European Parliament to back me up: those who want a strong Europe cannot shy away from this subject."

Greater financial flexibility provides us with greater political flexibility. And this is what we need if the EU is to fulfil its global commitments.

IV

One world – Europe's special responsibility

The European Union is the largest economic bloc in the world; it is the biggest donor when it comes to humanitarian assistance and development aid, and it provides a guarantee for stability, democracy and human rights. Europe must make an even greater effort than in the past to become a genuine global player.

Today Europe is already very active in the area of development cooperation with the poorest countries in the world, and does more than the U.S. or the Asian countries. It places special emphasis on Africa. The most important areas in which the European Union and its member states are involved are war, oppression, hunger, preventable diseases, the situation of women and children, the development of trade, the expansion of the infrastructure, education and the environment. We subscribe to the UN's Millennium Development Goals, which were discussed at the summit in September 2005.

However, development aid should not be confined to disaster assistance. It should facilitate sustainable development in the countries concerned. This is not only a humanitarian issue, it is also something which is in our own interests. We have this ONE earth and no other, we are directly and indirectly affected by developments in countries on the other side of the globe.

> "The ecosocial market economy is our response to the American way of life."

For this reason we wish to and indeed must make a contribution in this area, so that people in the most underdeveloped countries also have something to look forward to in their local communities. And that is why we support the initiative for a global Marshall Plan, an important partner on the road leading to the long-term goal of a global ecosocial market economy.

The successful model of European integration is the European form of the ecosocial market economy. In essence it consists of a synthesis of a competitive economy, social justice, and ecological responsibility.

The ecosocial market economy is our response to the "American way of life", it is the model of our European success, and constitutes an answer to the challenges posed by a globalized world. Furthermore, in global terms this is the model of the future, because it is the economic and social order which, even under changed circumstances, is capable of providing the greatest benefits for the individual human being.

The ecosocial market economy is in fact based on the idea that a free economic order which is surrounded by "railings" can provide the individual and society as a whole with stability, security, a sense of direction, and, in the final analysis, the freedom needed to attain growth and prosperity.

V

A new initiative

A demonstrable willingness to play a part in shaping the ongoing process of globalization is just as important as specific measures designed to reach the UN's Millennium Development Goals. For this reason I have made it unmistakably clear that I am in favour of a tax on foreign exchange transactions. An autonomous source of revenue would make the EU less depen-dent on the national budgets.

The Union's revenues originally consisted primarily of customs duties and levies, and only a small percentage came from national contributions calculated on the basis of GNI data. In 1989 gross domestic income (GDI) revenues constituted about a tenth of the EU's own resources. By the end of the current financial framework in 2013 the proportion will have risen to three-quarters. In the final analysis this is due to a decline in VAT-based revenues and in traditional own resources (in particular customs revenues, which have decreased and are decreasing rapidly as a result of GATT and WTO liberalization agreements). Thus, even if the budget were to increase only slightly, the proportion of GNI revenues would rise strongly. The question now arises of whether or not EU revenues should be placed on a more reliable footing.

These deliberations have led to a joint initiative by all the parties in the Nationalrat, the Austrian parliament. On 27 April 2006 the four parliamentary parties tabled a motion to discuss taxation proposals designed to finance supranational tasks such as EU own resources revenues, climate change, and cooperation with developing countries.

Selected Proposals for the Reform of the EU Budget

March 2007 **European Parliament report drafted by MEP Alain Lamassoure on the revision of the EU financial framework 2008/2009**
European Parliament

- By 2013: **abolition of exceptions** such as the British rebate, every state to contribute about 1% of its gross national income
- From 2014 onwards: **more EU taxation and reduced national contributions**. Possible sources: predetermined percentage of VAT, percentage of company taxation, energy consumption tax, Tobin tax, transport and telecommunications tax, European Central Bank profits

November 2005 **"The United States of Europe – A Manifesto for a New Europe"**
Guy Verhofstadt, Belgian Prime Minister

- An **EU tax** will make Europe less dependent on national budgets
- **Revenue neutrality**, i.e. what member states save on account of lower EU contributions must be returned to taxpayers by reducing taxation

December 2003 **"Letter of the Six" to the Commission**
"Group of Net Contributors"
Germany, France, United Kingdom, Netherlands, Austria and Sweden

- Opposed to a relative increase in EU budget
- **Capping EU expenditure** so that it does not exceed 1% of EU gross national income

July 2003 **Sapir Report**
Group of experts, economists and academics appointed by the President of the Commission, Romano Prodi

- **Criticism** of the structure of EU expenditure **and proposals designed to alter EU expenditure policy**
- Reduction in EU subsidies
  - **Reducing the extent of agricultural policy**
  - **Changing the nature of convergence policy**, so that, instead of subsidizing regions, the EU will channel aid to countries with a development backlog, and enhance the expenditure autonomy of recipients
- **More supranational finances** – new sources of revenue clearly associated with the EU

More financial resources are needed in order to reach the UN Millennium Development Goals. The proposed autonomous sources of revenue are designed to ensure that such resources will become available and that they will not be dependent on the national budgets.

In this motion, which is currently being debated in parliament, the parties in the

Nationalrat call on the Austrian government "in the context of its past initiatives within the framework of the European institutions to investigate the feasibility of an EU-wide tax, such as, for example,

- a tax on foreign exchange transactions,

- a tax in the areas of aviation, shipping, natural resources, etc.,

and to support consistent implementation, though without endangering the Lisbon targets.

The revenues thus procured will be assigned to an EU fund, which in an even-handed manner will finance supranational tasks such as EU own resources, climate change and cooperation with developing countries.

Implementation should be based on an EU directive, and be binding for all EU member states. Autonomous sources of revenue should be evaluated on the basis of whether or not they are consistent and consonant with free competition. The introduction of an EU-wide tax must be perceived in the European context and, when it is implemented, should not be permitted to distort competition. It is not supposed to constitute an additional burden for EU citizens, and will be revenue neutral on account of the simultaneous reduction in member state contributions."

VI

Exporting security

Security is a basic human need. The maintenance or reestablishment of security comes high on the list of what people value most. The desire for security is a fundamental aspiration of modern societies. It is in the first instance the task of the authorities of a nation-state to guarantee the security of a particular polity both externally and internally.
However, it has now become impossible to formulate security policy on an exclusively national basis or with reference to a single ministry. What is needed is international and cross-ministerial coordination and cooperation.

In the context of EU budget reform, some thought should be given to the question of whether, under the circumstances, sufficient funds have been allocated on a medium-term basis to deal with such issues – especially in the area of foreign and security policy.

Numerous security risks and threats to stability confront the EU, both in the immediate vicinity and in the more remote neighbourhood. On a global level there are various kinds of conflict. These range from the greater professionalism of international terrorism and the proliferation of weapons of mass destruction to regional crises and the consequences of failed states.

"Is the Common Foreign and Security Policy adequately financed?"

The new threats make it imperative for us to play a role beyond the confines of Europe in places where these developments have their origins. If we are not in a position to export security, we might very well find ourselves confronted with imported insecurity.

Each of these threats can be dealt with by combining a number of different policies. It is possible to contain the proliferation of weapons of mass destruction by imposing export restrictions and exerting political, economic and other kinds of pressure, whilst at the same time tackling the root causes of the problem. Combating terrorism may require a differentiated combination of diplomatic and economic activity, intelligence work, and police, judicial and military resources. In the case of failed states, there may be a need for military intervention to restore order and for humanitarian assistance if there is an emergency.

Regional conflicts require political solutions, but in the period after the end of the conflict there may also be a need for military resources and effective police work. Economic policy instruments can promote reconstruction, whereas civil management can help to re-establish a civilian government.

VII

The vision of global responsibility

Thus the EU's vision and its responsibility in the future must be to build on the stability which exists within its borders, to promote stability in its immediate geopolitical vicinity and in its more remote neighbourhood, and to make sure that it is sustainable. This is the key to peace in Europe in the 21st century.

But in order to be able to implement all the various aspects of this project, we need the appropriate financial resources. That is why there is such a pressing need for a reform of EU finances.

Responsible

Bertelsmann Stiftung
Carl Bertelsmann Straße 256
D-33311 Gütersloh
www.bertelsmann-stiftung.de/spotlight

dominik.hierlemann@bertelsmann.de
Phone +49 5241 81 81537

joachim.vannahme@bertelsmann.de
Phone +49 5241 81 81 421

Center for Applied Policy Research
Maria-Theresia-Straße 21
D-81675 Munich
www.cap.lmu.de

matthias.chardon@lrz.uni-muenchen.de
Phone +49 89 2180 1334

sarah.seeger@lrz.uni-muenchen.de
Phone + 49 89 2180 1375

ISSN 1865-7451

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