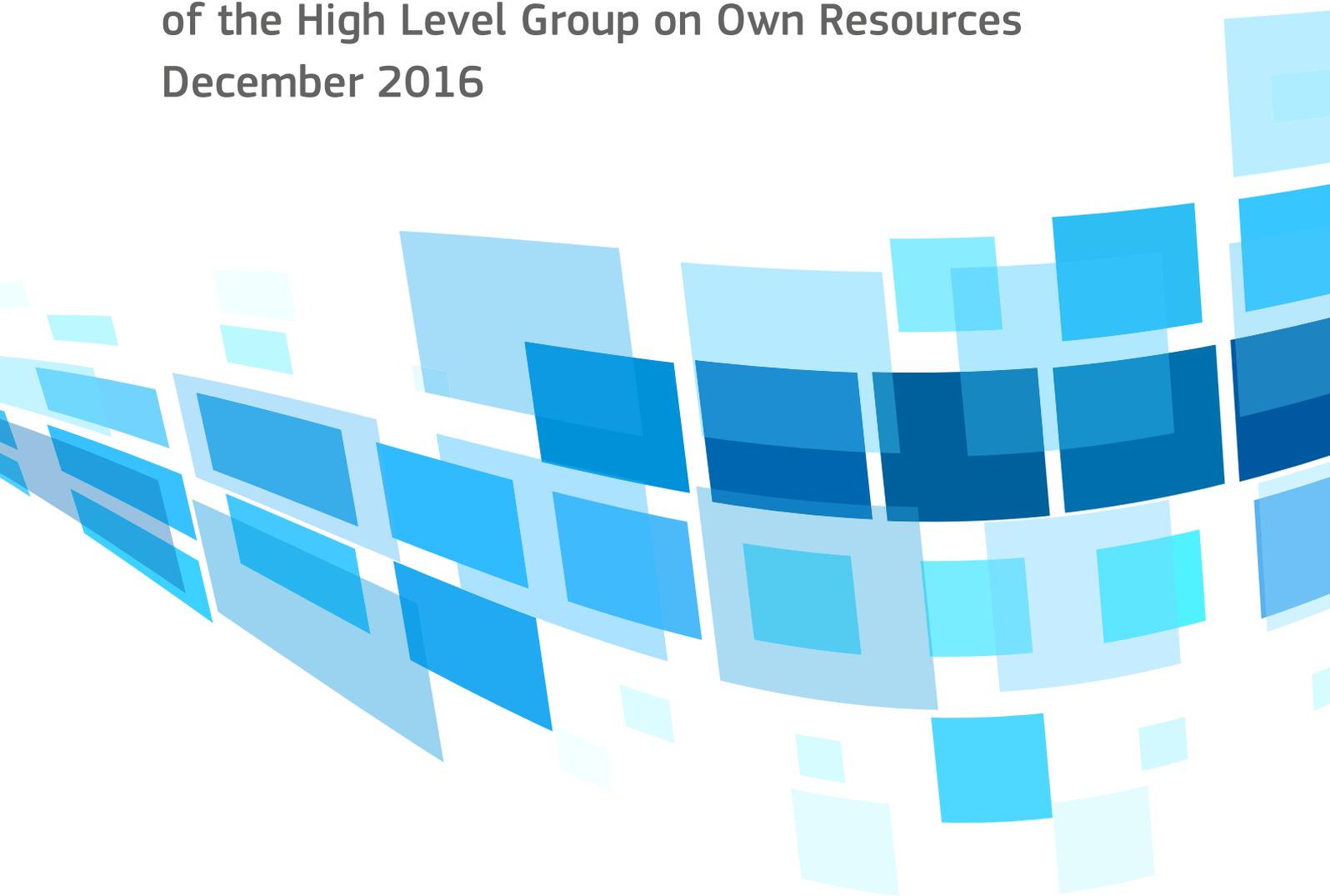


# FUTURE FINANCING OF THE EU

Final report and recommendations  
of the High Level Group on Own Resources  
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# Executive summary

## Genesis and mission of the High Level Group on Own Resources (HLGOR) and First Assessment Report

The High Level Group on Own Resources was established to examine how the revenue side of the EU budget can be made more simple, transparent, fair and democratically accountable.

The Group's First Assessment Report presented at the end of 2014 scrutinises the present system of own resources closely, with regard to its positive aspects and the substantial improvement needed, in terms of spending and revenue.

Criteria were developed to benchmark progress and questions were formulated to guide further examination. These went beyond the normal technical analysis of different sources of income, addressing the procedural and legal implications, and political and institutional interdependencies.

In the course of the deliberations of the HLGOR that took place in 2015 and 2016, the urgency and relevance of this examination were emphasised by multiple crises which served as wake-up calls that a much closer cooperation was needed at the EU level: the refugee crisis put in stark evidence the gaps in the Schengen zone of free movement; the multiple terrorist attacks in 2015 and 2016, most notably in France, revealed that more cooperative action had become imperative to ensure both the internal and external security of Member States; and not least, the existential risks associated with global climate change remind us that the EU is a Community of shared destiny for the long term and that, when this Community speaks with one voice and commits to common goals, it can influence global solutions. The EU has encountered great difficulty in addressing these challenges and redirecting EU capacity of action over the last years, which serves to underline how crucial financial resources have become in solving pressing issues internally and externally.

**The introduction and Part I** of the report explain why a functional EU budget is essential. They make the case

for a substantial reform, where changes on the revenue side are an integral part of a larger reconfiguration of the Multiannual Financial Framework (MFF). The report also mentions which aspects of the present system work well and should be maintained.

### The specific features of the EU budget, the MFF and the own resources system compared to national systems.

The observation that the EU budget is a 'sui generis' construction is not a ploy to hide its complexities. In the course of the debates of the HLGOR, it quickly became evident that much of the fierce criticism, mistrust and sometimes even misguided decisions stem from the wrong assumption that the EU budget is 'just' a 29th budget 'for Brussels'. This perception ignores the fact that the choices made concerning the EU budget are largely for the medium term.

The EU budget is primarily an investment budget with some redistributive functions between the Member States. It serves mainly to support common EU policies and objectives, underpinning the advancement of the *acquis communautaire* on a multiannual basis, and provides seed money for medium- to long-term investments. The flexibility and influence for short-term crisis intervention remains a weakness that must clearly be addressed. The budget is too small for real anti-cyclical economic stabilisation and substantive redistribution, which are a mainstay of national budgets, or for what orthodox wisdom would require of a 'federal-level' budget.

Finally, the budget must always be adopted as a balanced budget, which conditions the revenue system. Because of this requirement, the revenue is called so as to cover the expenditure voted by the European Parliament and

the Council each year (ex-ante at the level of payment appropriations). This means that the EU budget does not run an annual deficit, is not financed by borrowing money on the financial markets and thus does not build up public debt. In order to level out evolving needs on the spending side and imponderables on the revenue side, the uniform call rate for the residual, balancing contribution based on gross national income (GNI) is periodically recalibrated to cover the exact needs.

This last point is crucial to understanding what a reform of own resources along the recommendations presented by the HLGOR would lead to. Windfall income such as competition fines or higher than expected customs duties does not lead to additional spending possibilities, but to lower GNI-based contributions. The level of annually authorised appropriations, the MFF ceilings and the own resources ceiling are binding safeguards of budgetary discipline. The present report focusses on what can be reformed under the current institutional setup, taking into account that fiscal competences remain at the national level, and within the overall constraint of budget neutrality so that the reform of own resources envisaged do not create additional tax burden on EU citizens.

## Concepts and definitions, European added value, net balances.

The report clarifies conceptual issues and key notions, primarily to explain the differences between a 'European tax', own resources (some more 'genuine' than others) and other revenue sources. The treaties do not give the EU the competence to levy taxes but provide the Union with 'own resources' to achieve its objectives (Article 311 TFEU) while respecting the fiscal prerogatives of the Member States.

EU own resources, unfortunately, are interpreted in national budgets in a great variety of ways. This makes comparisons between Member States almost impossible and results in a conceptual bias where some own resources are in fact considered a national transfer or 'cost' item, and not a resource 'owned' by the EU. A first step towards more transparency would therefore be to acknowledge own resources for what they are, and provide a clear and standard presentation of contributions to the EU in national budgets.

The report also analyses how the notion of European added value, which can be defined as the value resulting from an EU intervention which is additional to the value that would have been otherwise created by Member State action alone, can guide future budgetary decisions on the expenditure side. Taking into account the most recent trends and developments in EU policies,

the analysis leads us to deduce that the EU budget is not as outdated as one might think, having undergone considerable changes, but that it is still insufficiently focused on the tasks that would generate the most European added value.

What is striking and unsustainable is that, when it comes to the basic data that each Member States uses to define its position in budgetary negotiations — its budgetary balance — European added value is completely ignored. Budgetary balances are calculated by simply offsetting what a Member State is allocated on the expenditure side with its national contributions. Under this method, every euro spent in one country is considered a 'cost' for everybody else. It therefore entirely ignores any European added value stemming from EU policies that benefit some or all Member States. Calculating one's own 'benefit' from the EU budget is not what is being condemned here; it is a natural or at least inevitable endeavour. What is misleading and causes damages to the EU and the Member States themselves is that a narrow and lopsided indicator becomes the only measurement of a cost-benefit relation.

The report argues that a broader measurement should be sought of the collective benefit of EU policies, economic synergies, cross-border effects and positive external outcomes. This would not only be more accurate, but would hopefully overcome the juste retour dilemma which has transformed the EU budget, and by extension the EU, into a zero-sum game instead of the win-win arrangement it is expected to be. Because this method was introduced to calculate the UK rebate, the withdrawal of the UK from the EU and the discontinuation of the 'British rebate' —as well as of 'the rebates on the rebate'— provide a unique window of opportunity to review how we measure the real costs and benefits of the EU.

## Part II discusses building blocks for a comprehensive reform and examines potential options

The Group has worked consistently with a set of criteria to assess and compare different types of revenue sources. Most of them are non-controversial and universally applied to public tax revenue, such as efficiency, sufficiency and stability of revenue sources. Others such as fairness are more complex to understand at EU level because of another essential difference to national budgets: under the current system, Member States are the only tax payers to the EU budget, not the 510 million EU citizens who only contribute indirectly. This explains why Member States generally strongly support the GNI-based own resource, which is seen as the benchmark of fair burden-sharing. As it is currently

implemented, however, together with the corrections and reductions granted to some Member States, it does result in a 'regressive' system. This fact, seen in relation to democratic accountability, is problematic. Looking at the EU budget from the point of view of the tax-paying citizen, or the consumer in the single market, would result in a different notion of 'fairness' leading to new forms of fiscal equivalence.

Some criteria are more specific to the EU, such as European added value and subsidiarity, which require the most mobile tax bases to be targeted by the highest level of European governance, as the national level is becoming increasingly less efficient at tapping them for fear of tax competition. This imperative of fiscal logic is, however, less easy to apply to the own resources system.

Finally, the report strongly argues in favour of new own resources which would help enforce some EU policies and support EU policy objectives, in particular economic, social and environmental sustainability. Some taxes or levies targeted to fight climate change or promote energy efficiency, for example, have long been recognised at the national level as ways to promote political preferences through taxation. A similar approach could be adopted if a coordinated tax were to be introduced in Member States, and some of its proceeds attributed to the EU budget. It would then participate in an EU policy. We have become used to the EU-level expressing political choices mostly through spending and subsidies. By better linking own resources (or other revenue) with common policies, this bias could be rectified.

### **The report confirms previous findings that there is no single ideal option, only several suitable ones.**

Alongside the elements of the current system which work well and should be kept, and the ones which should be abandoned, the Group examined in details several possible new revenue sources which have also been singled out by most analysts and academics. On this basis, a comprehensive and viable reform of the system of own resources could be based on a combination of new resources stemming from production, consumption and environmental policies. At this stage it appears more constructive to present a wide range of revenue sources having the required qualities rather than create unnecessary resistance to any specific option.

- » Possible new own resources related to the Single Market and fiscal coordination concern a reformed VAT-own resource (replacing the existing one), an EU corporate income tax, a

financial transaction tax and other financial activities' tax. These candidates would have the advantage of contributing to the better functioning of the Single Market and, particularly in the case of VAT and corporate income tax, promote fairer taxation and help combat tax fraud or tax avoidance, in addition to financing the EU budget.

- » Candidates related to the Energy Union, environment, climate or transport policies include a CO2 levy, proceeds from the European emission trade system, an electricity tax, a motor fuel levy (or excise duties on fossil fuels in general), and indirect taxation of imported goods produced in third countries with high emissions. These candidates would also contribute to the better functioning of the single market if they limit the proliferation of such taxes in an uncoordinated manner, and would create a link between the financing of the EU budget and EU policies.

Finally, own resources are not the only possible source of income for the EU. The category of other revenue has been neglected in past reflections but could become a complementary element in the financing basket. Other revenues stem directly from EU secondary legislation and could concern border control, the digital single market, environmental protection or energy efficiency (such as the excess emission premiums for cars which are already planned). Some of the candidates for new own resources mentioned above could also be candidates for 'other revenue', depending on the legal design envisaged and the possible political compromise.

### **Part III looks at practical ways forward, such as differentiation, before presenting the possible components of a global European financial reform, applicable to both the expenditure and the revenue side.**

Since the first ideas of differentiation were developed over 20 years ago, it has become a generally accepted solution that forward-looking policies which were not mature enough to be endorsed at the EU level, could be adopted by a coalition of the willing. Differentiation usually refers to a policy which is pursued by a core group of Member States which are both able and willing to go further, with the underlying assumption that other Member States will follow later.

This naturally has consequences on the revenue side, where there is already some measure of differentiation

for countries which make use of an opt-out, or countries which benefit from a rebate. The HLGOR has therefore examined this issue to define possible future options.

It recognises that a unified, universal and coherent way of financing the budget should remain the norm and that fragmentation of the EU budget entails many risks, particularly regarding democratic accountability and effectiveness. Any deviations should therefore remain an exception, be clearly justified and benchmarked against the usual financing of EU policies as laid down in the Treaty, which assumes that all Member States are participating, that the unity and universality of the budget are preserved and that decisions are taken according to the Community method and respect the specific features of the MFF and the Own Resources Decision.

The report then examines the circumstances under which differentiation could be justified. The treaties offer opportunities for frontrunners to make progress through the provisions for enhanced cooperation. A case in point is the Financial Transaction Tax, which was initially rejected at EU-28 level and has been brought forward by a group of 10 Member States. Further advances for euro area members could become another and the report points to particular sources of revenue which would be relevant in this context. Some differentiation might therefore be an element in the overall future compromise package.

The report concludes by proposing the possible components of a global European financial package, applicable to both the expenditure and the revenue side:

- » re-structure the MFF with more common public good spending focussing on achieving higher European added value and corresponding to the nature of the challenges;
- » introduce new own resources alongside traditional own resources and the GNI-based own resource, which would fulfil the classical sufficiency and stability criteria, vertical and horizontal aspects of 'fairness' requirements and also tackle policy objectives;
- » explore other revenue sources emanating from EU policies and programmes, which would be entered as simple revenue, rather than own resources, to the EU budget;
- » apply minimal procedural reforms;
- » include elements of differentiation, such as enhanced cooperation if strictly justified.

The upcoming negotiations on the next MFF will take place in a unique context: unprecedented scepticism

about the EU (and for the first time, the prospect of one of its Member States leaving); a widening gap between the main fields of EU action and the expectations of EU citizens; and calls for action in new areas which were not EU priorities until now.

While most of these challenges at first appear to concern the expenditure side of the EU budget, or areas which could be addressed by regulation rather than spending programmes, the long neglecting of how the EU is financed also explains why it is so difficult today to address the challenges we are faced with. Some argue that the strong support for the status quo on the EU financing structure — in particular from Member States — is merely an inevitable consequence of inadequate spending policies. Others argue the opposite — that policy inadequacies can be explained by an entrenched funding system. It is time to tackle this dilemma.

The reform of budgetary revenue is neither an end in itself nor a panacea to cure all budgetary ills. It should be seen as a building block in the ongoing effort to restore trust and legitimacy to EU action by making the EU's own resources system simpler, more transparent and equitable and democratically accountable.

# Recommendations

In compliance with its mandate, the HLGOR presents below its recommendations to the Presidents of the European Parliament, the Council of the European Union and the European Commission. The recommendations build on its First Assessment Report, on the external study it commissioned, as well as on discussions with national parliaments held at the Conference on the future financing of the European Union on 7-8 September 2016.

## #01

**A reform of the EU budget is necessary on the revenue side. It should be undertaken together with a reform of the expenditure side to address today's new priorities.**

The effectiveness of the EU general budget depends on the capacity — and the public perception thereof — to address EU priorities and to help solve the challenges our citizens face in their lives, be they economic, security-related and geopolitical, social or cultural.

This effort is not helped by the present system of financing, which has gradually become a system of national contributions where the EU budget is perceived as a zero-sum game between 'net contributors' and 'net recipients'. Moreover, such a system could create an unsustainable ratio between payments and commitments that needs to be closely monitored.

A reformed system of own resources should contribute to achieving our policy objectives, while also fulfilling its task of funding the EU budget appropriately, and easing the adoption of the budget. EU citizens deserve a budget that meets these challenges head-on whenever action at EU level is called for. The preparations for the next Multiannual Financial Framework (MFF) are about to begin. They will take place in a unique context which could help in overcoming the traditional obstacles to reform encountered on the revenue side. The next MFF will afford the opportunity to re-evaluate how the EU budget can support Member States and European citizens in a more efficient and effective way, and it is crucial to maximise on this opportunity. This should involve reflecting on the revenue side, and the size and composition of the expenditure, in order to match the objectives of and demands on the EU budget.

## #02

## The following principles should guide the reform:

- » European added value: In times of scarce public resources but growing financial needs, the EU budget needs to focus on areas bringing the highest 'European added value', or on European public goods for which action at EU level is not only relevant, but indispensable, or where national financing possibilities are insufficient for achieving our European goals. The Commission should demonstrate with concrete examples that a targeted, selective use of a central budget can lead to economies of scale, efficiency gains and better address external issues.
- » Subsidiarity: Changes to the composition of EU own resources should respect the powers of the national authorities to decide on them; on the expenditure side, any reform should include a subsidiarity test to determine the level at which spending should be best undertaken: sub-national, national or European.
- » Budget neutrality: The size of the budget is firstly determined by the own resources ceiling and secondly by the MFF, i.e. on the expenditure side. The structure of EU financing does not, as such, have an impact on the volume of the EU budget. The introduction of new own resources or other types of revenue would therefore — all other things being equal — result in reductions in GNI-based contributions, and could thereby create some margin of manoeuvre for national budgets or national fiscal policy.
- » Overall fiscal burden: New own resources do not aim to increase the fiscal burden for the EU tax payer. On the contrary, a reduction in national contributions, combined with EU spending that is better geared towards policies with higher added value such as security of external borders or defence, are also aimed at better European governance and can create savings for Member State budgets.
- » Synergies: Given constraints on the EU budget and the pressure on public expenditure in general, most European objectives should be sought through complementarity between the European and national levels. Greater attention should be given to synergies between the EU budget and national funding for areas with a high European added value or where national financing possibilities are insufficient for achieving a European public good. This approach is essential for restoring legitimacy to EU and public spending in general.
- » Unity of the budget: The unity of the EU budget should be explained and preserved, and 'satellite' budgets should be limited to strictly justified cases and subject to proper parliamentary scrutiny.
- » The EU budget and its financing should be more transparent and readable for citizens, so that the benefits of the EU, and not only its costs, are made visible. This would improve the overall accountability of the EU budget.
- » Own resources should not only be used to finance the EU budget in a sufficient, stable and fair manner. They should also be designed to support EU policies in key areas of EU competence: strengthening the Single Market, environmental protection and climate action, energy union, and reducing the fiscal heterogeneity in the Single Market.
- » Not only would a reform anchored in these guiding principles be completely justified, but it would also have the advantage of: providing a visible link to EU policies and priorities; improving overall budget coherence at EU and national levels; and promoting a sustainable financing system.

### #03

#### Some elements of the current system work well, are simple, equitable, efficient, and should be kept:

- » The principle of equilibrium of the EU budget, which is important in ensuring budgetary discipline, together with the own resources ceiling and the MFF.
- » Traditional own resources (customs duties), which are a benchmark of true EU revenue and whose collection process is satisfactory.
- » A GNI-based own resource, if used as a balancing and truly residual resource.

### #04

#### The most suitable options for new own resources.

The HLGOR conducted a thorough examination of possible options in the context of proposing a better mix of revenues with all the required qualities of a well-functioning, stable, transparent and fair system of own resources. The Group found that a comprehensive and viable reform of the system of own resources could be based on a combination of new resources stemming from production, consumption and environmental policies. The best options for establishing a link with EU objectives and added value would concern:

a. The Single Market and fiscal coordination: Reformed VAT-own resource (replacing the existing one), corporate income tax-based own resource, financial transaction tax or other financial activities' tax would have the advantage of improving the functioning of the Single Market. Moreover, particularly in the case of reformed VAT and EU corporate income tax, they would promote fairer taxation and contribute to the fight against tax fraud or tax avoidance — VAT being the only tax already covered by EU law.

b. The Energy Union/environment/climate/transport policies: the CO<sub>2</sub> levy, inclusion of the European emission trade system proceeds, an electricity tax, a motor fuel levy (taxes on fossil fuels/excise duties), or indirect taxation of imported goods produced in third countries with high emissions.

New own resources could be introduced with the new MFF. They could be phased in gradually or with certain pre-conditions, such as sufficient harmonisation of the tax base or an equitable transition to the new system.

The HLGOR considers that the objective of a future reform should be to finance the majority of EU expenditure via genuine own resources<sup>1</sup>.

### #05

#### Examine other possible revenues linked to EU policies.

Revenue other than own resources can also finance the budget and should be explored. For example, auctioning proceeds or other revenue stemming from EU policies such as border control, the digital single market, the protection of the environment or energy efficiency (excess emission premiums for cars), or resulting from EU competences, should in principle accrue to the EU budget, under the control of the European Parliament and the Council. Because these revenues have a direct link with EU policies, they are visible and simple. Their use would have to be decided on a case-by-case basis. They would be used either to finance the general budget and simply decrease the national contributions or create a reserve on the expenditure side, or be earmarked for a specific purpose.

1. One member of the group thinks that, under the current institutional framework of the EU, abolishing the VAT based own resource and simplifying the system of national rebates would considerably improve the financing system in the light of the relevant criteria while the case for adding new own resources is much weaker.

#06

## Aim at a more comprehensive and accurate notion of ‘costs’, ‘benefits’ and ‘net balances’.

The current perception of the EU budget as a zero-sum game does not reflect the European added value dimension of EU policies, and tends to favour pre-allocated expenditure by Member States to the detriment of current or future EU policies with clear European added value such as internal and external security, combating climate change, research and defence. Naturally, it does not take into account benefits, which are not measurable either, such as participation in the largest single market or belonging to one of the heavyweights in world trade and climate negotiations.

The Group recommends addressing this problem in two ways. The first is to introduce alternative revenue sources, which are not perceived as national contributions but rather as resources directly linked to the European dimension.

The second is to look critically at the current methodology of net balances, which was introduced to calculate the UK correction, and develop additional indicators or tools beyond the current calculation of net balances that allow for a more comprehensive appraisal of the costs and benefits of EU budgetary interventions. Such methodology and/or additional indicators need to better reflect the collective benefits of EU expenditure, as well as the costs and benefits per Member State. These costs and benefits include the financial flows triggered by EU budgetary interventions in Member States, such as the investments linked to EU financial instruments, or by other forms of EU financial assistance. This will show that one Member State’s gain is not inevitably at the others’ cost. A study should be commissioned to this end.

#07

## Corrections and rebates.

Withdrawal of the UK from the EU entails the discontinuation of the UK correction mechanism and the related ‘rebates on rebate’. This in turn makes much of the rationale for the present statistical VAT-based own resource superfluous.

More generally, any correction mechanism on the revenue side should be abolished. The balance between own resources has to be so that we can avoid any correction mechanism. In case of any excessive burden caused by one or another own resource on a Member State, it could be alleviated by means of a specific compensation limited in duration and amount, and preferably calculated in terms of lump sums. Such an approach would make the own resources system simpler and fairer.

#08

## Review the vertical coherence of the EU and national budgets within the European Semester.

It is recommended that the link between the EU budget and the overall fiscal policy governance framework be strengthened in order to create synergies and minimise the fiscal burden where possible.

On the expenditure side, the coherence of EU and national budget spending would be a key point of any reform, taking into account several principles — the need to have expenditure at the right level (EU or national), the identification of common objectives for both EU and national budgets and the quality of public finances (growth-friendly expenditure).

On the revenue side, better information channels should be opened in relation to national budget procedures, the European budget procedure and the European Semester so that national contributions to the EU budget are clearly understood and anticipated, and shared objectives better aligned. A comparable budgetary and accounting presentation of own resources in national budgets would be a first step in this direction, and would facilitate parliamentary scrutiny.

#09

## Allow for a certain degree of differentiation (géométrie variable).

The fundamental budgetary principles of unity and universality of revenue should remain the 'point of departure' of any reform effort and not be jeopardised. Only when some Member States wish to go further in some areas of EU integration, differentiation on the revenue side could be a workable solution, notably:

- » for the further development of the euro area. Earmarking such revenue sources for specific items of expenditure would also be easier to justify in this context. Some candidates examined by the Group could be suitable for the euro area, such as the financial transaction tax, possible contributions from the banking sector or the income from seigniorage stemming from the European Central Bank.
- » for policies under enhanced cooperation where there is a coalition of frontrunners (new policies such as defence).

The HLGOR considers that these recommendations are compatible with the current European treaties and could be implemented under the next MFF. Where the report addresses some forward-looking ideas which could only be implemented through a Treaty reform, this will be clearly stated. In any case, it should be borne in mind that changing the own resources decision requires the unanimous agreement of Member States, after consultation of the European Parliament, and ratification according to national procedures.

# INTRODUCTION

## The need for a solid EU BUDGET

The High Level Group on Own Resources (HLGOR) hereby submits its final report and recommendations concerning the future financing of the European Union, as mandated in December 2013 by the European Parliament, the Council and the Commission<sup>2</sup>. The Group was created in the aftermath of the previous negotiations on the multiannual financial framework, at the specific request of the European Parliament, in order to examine once again the EU financing system and see whether and how a reform could finally find support among all Member States after decades of failed attempts. It started its work in April 2014 after the presidents of its three parent institutions jointly designated Mario Monti as its Chairman and after each institution designated three members to contribute in a personal capacity to its work.

Political reporting on the work of the Group has been ensured periodically in different settings of the European Parliament and the Council, and led to interesting discussions with national parliaments at the Conference of 7 and 8 September 2016 in Brussels. In addition, the Group's reflections benefited from many consultations and hearings of experts, some of whom even updated and expanded their analysis specifically to answer the questions and concerns raised in the First Assessment Report, as well as from an external study commissioned from a consortium of researchers led by the Centre for European Political Studies (CEPS)<sup>3</sup>.

### The EU budget, what is it good for?

This basic question should be revisited every once in a while. A viable proposal for the reform of the own resources system and a productive debate about its merits hinge on a solid and up-to-date understanding of the purpose and functions of the EU budget.

Since the sobering verdict qualifying the EU budget as a 'relic from the past' more than 10 years ago, substantial reforms have been undertaken and imbedded in the

policies adopted under the respective 2007-2013 and 2014-2020 multiannual financial frameworks, in particular to increase the added value of EU policies. There is still, however, a lot more work to do for EU policies to perform better.

At the same time, the EU has gone through some of the more turbulent and difficult times since its inception. The financial, and economic, crisis of 2007-2008 has seriously threatened the existence of the euro. And the ensuing debt crisis of several euro area countries (Ireland, Cyprus, Portugal, Spain and most prominently Greece), and non-euro area countries (Hungary, Latvia and Romania, for a shorter period) have dominated the European agenda for years, leaving insufficient time and attention to be devoted to EU reforms.

Yet other priorities have emerged, some since the High Level Group started its work, which were unforeseen a few years ago, at least in their degree of urgency: the refugee crisis has put in stark evidence the gaps in the Schengen zone of free movement, and the multiple terrorist attacks in 2015 and 2016, most notably in France, served as wake-up calls that much closer cooperation was needed in terms of both internal and external security, at EU level.

In addition, the existential risks associated with global climate change underpins all of these priorities, and for the long term.

All these crises have put the emphasis on areas that economists have also been telling us for years that the EU should focus on (because these are where the potential highest added value is). A consistent and large majority of EU citizens also support action at the EU level in these areas where it is felt that nations alone cannot act efficiently. However, the EU as we know it, and the EU budget even less, is not equipped to deal with them with all the strength it can show in its other, full-fledged, more traditional competences.

2. See Annex 1 — Joint Declaration on Own Resources and Annex 2 — The work of the HLGOR in detail.

3. Study on the potential and limitations of reforming the financing of the EU budget, 3 June 2016, CEPS, Université de Pau et des Pays de l'Adour, LSE Enterprise and Deloitte (Jorge Núñez Ferrer, Jacques Le Cacheux, Giacomo Benedetto and Mathieu Saunier).

4. 'Sapir Report' (2004): to be fair, the Sapir Report devoted only a few paragraphs to the functioning and structure of the EU budget and mostly focused on growth in Europe in general. Since then, several studies

Some of these areas represent the conventional core of national sovereignty, in particular internal and external security. While they have led to increased cooperation at the EU level, this has often entailed some degree of 'géométrie variable' where some Member States have chosen to participate on a voluntary basis or to opt-out altogether. Such differentiated arrangements, deviating from the community method, can make the recourse to the EU budget more difficult, and in any case contribute to its complexity (see Annex IV).

In some cases, the recent crises have revealed the limitations of the multiannual financial framework in accommodating the budgetary needs arising from new responsibilities that European leaders — gathered in the European Council — have themselves entrusted to the Union, such as the Juncker Plan, migration policy, security policy, follow-up on the COP21 and the climate change negotiations. These new responsibilities have led to the creation of ad hoc funds or instruments parallel to the EU budget with ad hoc decision-making procedures (and different accountability).

The EU is therefore under strong pressure to intervene in areas other than its traditional core business, and not according to its well-established rules and procedures. This may help address emergencies and find financing when there is not enough support to revise the financial framework or use the EU budget. But it also creates an unprecedented conjunction of risks for the Member States and the EU altogether, if they fail to address these challenges.

The case for European added value in these new areas of action is crucial precisely because their financing is ad hoc. It is not as solidly anchored as the expenditure financed from the MFF and the EU budget, which have undergone — at the EU level — a democratically accountable process that leads to consent to taxation and transparency in the use of tax revenue (in this case, the consent to finance from own resources).

This is not to say that the test of European added value should not be undertaken for all policy areas, including the well-established ones like agriculture and regional policy. On the contrary, this test is crucial to help identify where budgetary margins of manoeuvre can be found to finance new actions and policies, and where the financing of current policies can be improved. Moreover, financial intervention is not the only tool at the EU's disposal. Under certain circumstances, it may be advantageous to implement a common policy via diverse sources of financing.

When reflecting on a future reform of EU financing, it is important to take into account the specificities of the EU institutional framework which make the EU budget unique and different from budgets at the national or regional and local level:

- » There is a double constraint on EU spending: the own resources ceiling (1.20% of the total EU GNI<sup>5</sup>) and the multiannual financial framework's annual and overall payment ceiling (EUR 1 025 billion for 2014-2020 and, for example, 144.7 billion in 2016). The EU budget must respect both and is always in balance; it cannot be financed by debt.
- » The Own Resources Decision (providing for both the own resources ceiling and the different categories of own resources) is decided at unanimity by the Member States and ratified by national parliaments.
- » There are presently three types of own resources: customs duties, the VAT-based own resource and the GNI-based own resource. The latter plays the role of the residual resource: it is calculated once the other two are known, in order to ensure that the budget is balanced. It now represents about two thirds of the total of own resources.
- » The power to tax and the choice of the fiscal mix remain at the national level. Changes in the composition of own resources do not necessarily imply changes in what citizens ultimately contribute to the EU budget. But it could create the conditions for Member States to change their fiscal mix if they so wish, for instance by alleviating taxes on labour using the amount freed from reduced GNI contributions.
- » The European Parliament is only consulted on own resources, but must give its consent on the multiannual financial framework, and co-decides the annual EU budget. There is a clear asymmetry of power embedded in the system.

As long as this institutional set-up is maintained, the scope for reforms, in particular the scope for introducing anything resembling an EU tax, which would establish a more direct link between citizens and the EU budget and induce more democratic accountability in EU financing at EU level, is limited. This would be different if the institutional set-up of the EU was changed or EU fiscal competences were introduced, with a European Parliament that would have real tax-raising powers and no fixed ceiling for EU spending. Whether or not

5. Previously: 1,23% of GNI; the own resources ceiling has been recalculated to 1,20% of GNI with the coming into effect of the new ORD and the switch to ESA2010 for the definition of GNI in the EU.

such a step is desirable is a very fundamental political question.

However, the present report focuses on what can be reformed under the current institutional set-up, taking into account that fiscal competences remain at the national level, and within the overall constraint of budget neutrality so that the reform of own resources envisaged do not create additional tax burden on EU citizens. In addition, some reforms on the expenditure side, centred on providing the essential services and public goods that EU citizens are expecting the EU to deliver, should lead to savings at the national level.

### **Within this general context, how can the EU budget deliver on the new priorities that have emerged in the last decade?**

Article 311 of the Treaty provides that 'the Union shall provide itself with the means necessary to attain its objectives and carry through its policies.' It is often stressed that the financial resources of the EU budget are only one of the 'means' necessary. The regulatory and political dimension of EU interventions, the single market with its four freedoms, the 'single voice' in international trade negotiations, the projection of European influence in key issues of international affairs, ranging from the Middle East Peace Process to sanctions against Russia or the UNFCCC climate regime: all of these do not necessarily require large amounts of budgetary resources.

However, many of these assets have to be underpinned by financial means and many of them will be much more effective if fleshed out and accompanied by EU budget programmes.

The Interinstitutional Conference with National Parliaments of 7 and 8 September 2016 emphasised several distinct purposes of the EU budget which should be at the core of the reform debate: the multiannual investment nature, the leverage potential (with several facets) and 'trouble-shooting' at the appropriate level:

- » Investment and multiannual programming: the medium-term nature of EU programmes gives stability and fills an essential gap that national budgets and private investors often leave open. This should not be traded lightly for short-term objectives or crisis management only.
- » Leverage: the EU budget can be a successful 'lever' and not only through a financial vision, such as when it offers guarantees to public and private co-funding in the EU. As a public budget,

it can also have a more political dimension in the noble sense:

- investing in more risky ventures which would perhaps be shunned by the private sector (fundamental research for example);
  - funding and co-funding programmes that fulfil the commonly agreed European objectives as a priority;
  - preserving and developing the EU's energy and environmental acquis, research and innovation policy, cooperation in the area of Justice and Home affairs;
  - linking EU financing instruments with sustainability agendas or national reform programmes;
  - linking international and development action to compliance with human rights.
- » Trouble-shooting, crisis management and providing security at the appropriate level. The EU budget needs to be sufficiently versatile. The mid-term review of the MFF has just proposed to further reinforce the budget devoted to migration management and security to complement the action of Member States. The recent launch of the European Border and Coast Guard is a case in point.

There is always a tension between the predictability and the responsiveness of the EU budget, and the balance needs constant re-adjustment. From the point of view of the HLGOR, the revenue system should also contribute to this adjustment and not stand in the way when the EU needs flexible response. It is a minimum requirement and one of the remarkable features of the current revenue system that, once a new and un-programmed action is agreed to respond to a crisis, sufficient revenue will be found for it.

Finally, the Interinstitutional conference with National Parliaments pointed out another innovative viewpoint: the revenue side can also contribute to added value, co-benefits and leverage, aspects which were mainly applied to expenditure until now. The 'link to policy' has been one of the most neglected criteria of the present own resource system, even though this is a 'normal' policy tool at national level. It deserves closer attention.

Taken together, these purposes provide a forceful rationale to dedicate at least one percent of our collective prosperity to the central EU budget.

# PART 1 — THE CASE FOR REFORM (AND CONCEPTUAL CLARIFICATIONS)

## 1.1. EU expenditure and revenue: two sides of the same challenge?

The Council's dedicated website on EU policies describes the MFF as having four purposes: 'The purpose of the MFF regulation is to:

1. make the adoption of the annual EU budget easier
2. translate political priorities into figures for a budget cycle of at least five years
3. ensure budgetary discipline for the EU
4. add predictability to EU finances.<sup>67</sup>

The **first purpose** has certainly been fulfilled for a long time: all annual budgets since 1988 have been timely adopted, ending more than a decade of budgetary conflicts between the European Parliament and the Council (budget years 1980, 1985, 1986 and 1988 had to start under provisional twelfths). Some argue however that in recent years, and notably since the MFF was enshrined in the Treaty and the annual budgetary procedure changed (new Article since Lisbon), some annual budget procedures are less smooth and could only be closed successfully after excessive drama. Are these problems solely symptoms of a running-in period or are they a symptoms of a more serious dysfunction?

The **second purpose** is the most challenged today. Political priorities are set out, modified and sometimes receive precise guidance from Heads of States in their European Council conclusions. They are then enacted through EU legislation adopted by the European Parliament and the Council, and implemented by the Commission. Harsh criticisms have been formulated by academia and media of the gap between the commitments and promises on the one hand, and the reality on the ground (Sapir Report 2003), most vividly concerning grand strategies such as the Growth and Jobs strategy, the achievement of the millennium goals, or the EU 2020 strategy for smart, sustainable and inclusive growth.

The **third purpose, budgetary discipline**, is ensured by three different safety belts. The first and most

stringent one is the Own Resources Ceiling, which sets the maximum amount of own resources which can be called from the Member States each year. It applies to the EU appropriations for payments. This ceiling is set at 1.20% of the gross national income (GNI). The own resources ceiling, for all practical purposes, is an upper limit. It is adopted at unanimity by all Member States, requires consultation of the European Parliament and ratification by all national parliaments. Given the difficult procedure to adopt it, the ceiling is therefore very stable (see Annex V). The second safety belt ensuring EU budget discipline is the existence of the MFF itself, as each political priority (heading) is constrained by a maximum annual amount (ceiling). The MFF applies to both commitments (one annual ceiling per spending category) and payments (one global annual ceiling). The MFF is set for a period of at least five years (currently seven years). It is adopted at unanimity by all Member States and requires consent of the European Parliament. Thirdly, the EU annual budget is adopted each year by a joint decision of the European Parliament and of the Council, the latter voting by means of a qualified majority. In practice, the voted and executed EU budget has stayed significantly below the own resources ceiling and important margins were until recently left below the ceiling (see the graph in Annex V on the evolution of the own resources ceiling, the MFF ceiling and the payments executed since 1988).

The **fourth purpose — predictability** — covers two aspects: the predictability of the evolution of EU expenditure which stems from the multiannual budgetary discipline; and, more essential for national governments, the predictability of their annual contribution to the EU budget which is mainly determined by the own resources system.

Due to the requirement of having a balanced budget, and unlike in national budgets, the revenue side must be recalibrated every time the level of payment appropriations changes and when the forecasts of own resources, e.g. custom duties, are updated to match real income in the course of budget execution. Predictability of EU expenditure therefore has to be seen within this fluid context. It has some solid points of reference such as the own resources and the MFF ceilings, but it cannot

6. <http://www.consilium.europa.eu/en/policies/multiannual-financial-framework/>

7. Council Regulation (EU, Euratom) No 609/2014 of 26 May 2014 on the methods and procedure for making available the traditional, VAT and GNI-based own resources and on the measures to meet cash requirements (Recast).

be ensured in an absolute manner. Recent amendments to the ‘Making-Available Regulation’<sup>7</sup> have already led to a significant simplification for national treasuries by allowing for a certain ‘netting’ of cumulative effects of adjustments on the revenue side and thereby decreasing the number of amending budgets.

Moreover, ‘predictability’ is often at the losing end of trade-offs, and with reason: the annual adjustments — and sometimes additional ad hoc adjustments — of the revenue distribution are made for the sake of ‘fairness’, for example in order to better reflect the latest evolutions in the GNI base. This is done in full transparency with the input and assistance of the Advisory Committee on Own Resources.

In order to improve predictability for national budgets, there are certainly some steps to be taken to ensure more regular and specific information flows so that the EU budget procedure becomes a more organic element of national budget procedures and mutual understanding is improved<sup>8</sup>.

The dilemma which results from the above is that, while the discipline is mostly ensured on the expenditure side with the existence of the MFF, budgetary negotiations mostly focus on the resulting national contributions from expenditure, as forecasted for the duration of the MFF (currently seven years), and not on the nature of expenditure themselves. This makes it extremely difficult for the EU to address new priorities with a financial impact in a fast-changing world with changing priorities, such as has been the new reality of the EU post-2008 crisis, and even more in the last three years. Annual budgets are in fact tightly locked in the structure which has been decided for seven years. There is only a very limited margin of manoeuvre possible, and from which the two biggest areas of expenditure — agriculture and cohesion — are shielded.

On many occasions in the past, Member States managed to accommodate significant changes or new priorities by revising the multiannual financial framework, either with a qualified majority if the change amounted to less than 0.3% GNI, or at unanimity above that percentage. Revisions in most cases benefited from the existence of comfortable margins under the ceiling, even if there was always, as much as possible, an offsetting of margins. Today, with the revision of the MFF being only possible at unanimity, and with shrunk margins, adjustments can be made via other means such as the use of the global margin for commitments (GMC), the contingency margin (CM) and the global margin for payments (GMP) which have made revisions like those in 2007-2013

superfluous, so far at least. While these new procedures are less visible and somewhat more complex, they have proved efficient in recent years.

The mid-term review of the multiannual financial framework 2014-2020, which was presented on 14 September 2016, recapitulates how these special instruments are being put to use: the contingency margin and the global margin for payments were used to adjust the payment profile in 2014 and 2015 and the global margin for commitments has allowed for the frontloading of the EU budget share used as the guarantee for the European Fund for Strategic Investment. Finally, the contingency margin will be used in 2017 to reinforce the EU policies on migration and security.

## 1.2. Are own resources some kind of EU tax?

The following chapter sets out to provide terminological clarity and offer some definitions of key notions. This is particularly important because EU financing reflects the hybrid nature of the EU, with some elements being more intergovernmental and others more supranational, while substantial changes to the financing provisions may have a much larger impact in the long-term. In addition, the internal discussions and outreach activities of the Group have revealed that, despite the vast body of information available, there are often inadvertent (and occasionally mischievous) misconceptions about the financing of the EU budget. This has sometimes injected elements of confusion or irrationality into the negotiation process.

### 1.2.1. What is ‘owned’ by the EU? What is an own resource and how is it different from a tax in the sense normally used to describe the main fiscal instrument used at the national level?

#### 1.2.1.1. The decision to attribute resources to the EU

Article 311 of the Treaty provides that ‘the Union shall provide itself with the means necessary to attain its objectives and carry through its policies. Without prejudice to other revenue, the budget shall be financed from own resources’.

8. Since the inception of the HLGOR, legislative amendments to the so-called Making Available Regulation have been enacted which will simplify the year-end balancing exercises and result in a lower number of amending budgets.

*The EU does not have the power to levy taxes. Only national authorities do.*

Clarifying this question is not simply a rhetorical exercise to be discussed between experts. It is all the more important to be clear what we are talking about because of the sensitivity of the word 'tax', and on the quality attached to it as one of the last expression of sovereignty. The EU does not have the power to levy taxes. This competence is the exclusive realm of Member States and the Treaty clearly recalls that fact. Thus, talking about an 'EU tax' or mislabelling the EU's own resources as EU taxes without further specification may not only be incorrect from a legal point of view, it fuels suspicion and incites criticism towards any attempt to reform the system of own resources by making policy makers and citizens believe that there is a hidden agenda behind such reform.

The Group wishes to be extremely clear that the proposals for reform it promotes can be implemented within the current Treaty framework, without compromising the Member States' fiscal competences whatsoever. There would, of course, be other scenarios possible if a Treaty reform on this point was to be envisaged, but this is neither a precondition for a better system, nor does it appear desirable in the current context to devote a large chunk of political and institutional time to such a long and uncertain process.

Thus, given that tax competences remain with national authorities, the Union's own resources can be defined as revenue allocated irrevocably to the Union to finance its budget and accruing to it automatically without the need for any subsequent decision by the national authorities. The initial decision to attribute any particular source of revenue remains a national competence, and this is expressed in the clearest manner by the decision-making process applicable to own resources, which requires both unanimity in Council and ratification by all Member States in accordance with their respective constitutional requirements, whether this means a vote by the national parliament concerned, a referendum or any other due process. This is a very similar decision to the one a central government would take in order to attribute some fiscal revenue to decentralised regions or smaller geographical entities so that they can effectively implement their devolved competences and responsibilities.

*Own Resources provide more reliable and stable revenue. Their amount is established once the budget is adopted.*

Only after the approval of all Member States will the own resources decision enter into force. At that point the identified source of revenue is 'owned' by the EU. This is one of the most original features of the EU financing compared to international organisations such as the United Nations for example, which depend for their financing on the annual contributions by Members, and therefore also on possible national power games, to the detriment of stability and predictability of the policies of the entire organisation. The elaborate system established in the regulation which lays out the detailed provisions to make own resources available to the EU serves as a very efficient deterrent against such power games because it makes them costly: steep interest payments are laid down in legislation for any late payer. It also explains how the EU is able to maintain a very high credibility as a good payer in the international context. As an indicator of this, the EU kept its triple A rating as assessed by the main rating agencies even in the darkest hours of the 2007-2008 financial crisis.

In the present system of own resources, the decision of attribution is taken with the entry into force of the Own Resources Decision, which is usually revised with each new multiannual financial framework, hence for a period of at least five years (currently seven years). The consequence of this attribution is that, when the annual budget of the EU is adopted each December, the revenue side is automatically calculated and adopted on the basis of the annual expenditure voted in order for the EU budget to be in balance, which is a Treaty obligation. Actually, the argument should go even further: because the attribution of own resources is decided according to the most stringent procedure (unanimity plus ratification), an additional and annual decision on the same attribution would be contrary to the Treaty because it would be made according to the less stringent adoption procedure of the annual budgets (qualified majority in Council and co-decision with the European Parliament).

For this very reason, the way the GNI share of own resources is sometimes instrumentalised in annual negotiations leads to the questionable practice where some Member States consider it as a transfer from their national budget, and thus open to negotiation, whereas as an already attributed own resource it should not be questioned in this context. It is the belief of this Group that such practices bring only confrontational and fruitless outcomes, and that we should collectively refrain from them.

A way forward to bring back some rationality to this issue would be to address the heterogeneity of the way EU own resources are presented at national level, in particular in national budgetary documents.

### 1.2.1.2. How this decision of attribution is interpreted in national budgets

*Only four countries present own resources for the EU in their national budgets as what they are. Most other countries count them as public expenditure.*

The way national budgets present their share of EU own resources is very indicative of the fact that Member States mostly consider the GNI share of own resources, and sometimes the VAT-share as well, as transfers from their national budgets. As a 2014 study commissioned by the European Parliament shows, only four countries actually internalise the notion of own resources on the revenue side of their budget and 'classify the EU contribution as an attribution of national receipts to the EU, in line with the original design of the system of 'own resources'.<sup>9</sup> They do not count such revenues first as government income.

And these four countries do not necessarily use the same rationale or concept: in France, part of the revenue is attributed to the EU ('prélèvement') in a manner similar to revenues raised for French regions. In Germany, the resources for the EU are attributed ('EU-Eigenmittel'). In Austria, EU income is considered as a reduction of earnings and deposits to public expenditure. Finally, in Bulgaria, a share of tax receipts is attributed to the EU alongside the contributions to international organisations.

The 18 other countries examined in the study record the revenues attributed to the EU as a direct public expense, with marked differences as well. Belgium and Luxembourg record VAT-based contributions as attribution of receipts, but GNI-based contributions as expenditure. In the Czech Republic, Denmark, Estonia, Ireland, Spain, Italy, Cyprus, Lithuania, Hungary, the Netherlands, Poland, Portugal, Finland and Sweden, contributions to the EU budget are recorded as expenditure of the government, but in various categories of spending. Finally, in the United Kingdom and Romania, the net concept is applied directly: in the UK, the rebate is deducted from the theoretical gross contribution, and the resulting net contribution is presented as a transfer from the UK Exchequer to the EU; in Romania, only the net contribution is shown.

This heterogeneity does not only make comparisons difficult, it perpetuates a misleading perception of the revenues attributed to and the receipts stemming from the EU budget, often reduced to a simple 'costs' and

'benefits' vision, which makes it almost impossible for citizens to have a clear view of what their country's contribution actually is. The use of net balances as 'expenditure', in particular, is highly distortive because some funds only transit through the budget.

As far as the 'benefits' from the EU budget are presented in national budgets, they are as diverse and patchy and result in a very complex picture. 'Generally, Member States do not estimate the benefits in terms of economic impacts from the EU, which may be many times larger than the purely monetary costs'. And while the European Commission publishes in its annual Financial Report the estimated figures for all Member States' receipts resulting from the EU common policies, only the United Kingdom, Austria, the Czech Republic, Lithuania and Romania present such consolidated estimates in their national budget, notably for the common agricultural policy, structural funds and research (the previous R&D framework programme and now Horizon 2020).

The study recognises that the difficulty of showing the receipts from the EU budget in a reliable manner is increased by the fact that central governments are not the only recipients: regions and local governments, public and private enterprises, and in some cases citizens (Erasmus grants) also may benefit directly from EU policies. For this reason, the study considers that any 'classification of receipts from the EU budget may therefore best be left to the Member States'.

However, the diversity of national institutional systems and of fiscal relations between central governments and local entities does not play a role in the presentation of the 'costs' of the EU in national budgets. The study thus calls for a consistent and harmonised handling of Member States' contributions as an attribution of government receipts and not as expenditure. This would be essential to put more rationality and transparency in budgetary debates, increase accountability and would facilitate comparisons. It would perhaps encourage, in time, the presentation of a more exhaustive picture of the benefits from the EU budget as well.

The Group shares the conclusion that the handling of EU own resources in national budgets should be improved, and if possible presented according to an agreed set of principles.

As a first step, the analysis needs to be completed to cover all Member States and data relating to both budgetary and accounting categories used to present EU budget information in national budgets.

As a second step, a common standard of presentation should be discussed and agreed by Member States, hopefully in time to be implemented with the next

multiannual period. The 'national contributions' to the EU budget should not be recorded and presented in national budgets (next to other expenditure items) as if there were any discretion to change them in the national budgetary procedure. This would increase transparency and visibility of the Own Resources system, and thus facilitate parliamentary scrutiny, which is one of the objectives of the present report. It would also encourage, on the expenditure side, a reflexion on how 'benefits' or impacts from EU financing are presented.

*RECOMMENDATION 8 - the accounting presentation of own resources and in particular 'national contributions' in national budgets should be harmonised: they should be considered as an attribution of governments' receipts and not as expenditure, and presented on the revenue side.*

## 1.2.2. Are some resources more 'owned' than others? The legal interpretation

Beyond the general definition of own resources given above, a more detailed examination of the current system shows there are differences between the various own resources, which explain why some are more genuine than others. Legally, such differences are repressed. Article 311 of the TFEU simply stipulates: 'Without prejudice to other revenue, the EU budget shall be financed by own resources'. The Own Resources Decision (ORD), which enacts the Treaty provision, explains that the sources of revenue adopted according to the Treaty procedure constitute revenue allocated irrevocably to the Union to finance its budget and accrue to the EU automatically without the need for any subsequent decision by national authorities. The ORD makes no categorical distinction between the different types of own resources, notably, the traditional, VAT-based and GNI-based own resources.

'Own resources' can of course simply be construed as any sort of revenue which is defined as such in the ORD, regardless of its other inherent characteristics or merits. The EU budget documents and the Financial Regulation broadly use the term 'own resources' in this sense. The budget nomenclature clusters own resources (TOR, VAT-based, GNI-based) in title 1 of the General Statement of Revenue and separates them from 'other revenue' such as surpluses (title 2) or interest on late payments and fines (title 7) which are not taken up in the ORD.

*Most academic analyses agree that only traditional own resources (customs duties) qualify as real own resources.*

However, the large body of academic analyses which try to tackle the definition of an own resource, from those centred on fiscal federalism theory, to those more specific to the EU and its history, all agree on one element: among the current 'EU own resources', only the traditional own resources qualify as such in the narrower sense of the term. There are several reasons for this:

- » The decision-making in the policy area underlying TOR (customs) is largely based on the community method.
- » Financially, the incidence as well as the proceeds of TOR cannot be easily attributed to any particular Member State. Countries where the main ports of entry are located (Belgium, the Netherlands) — and thus where significant TOR are collected — have sometimes voiced the argument that their share in TOR is too high. However, while this reflects their advantageous position at the core of the customs union, the costs of the custom duties are carried indirectly by companies and individuals from the whole EU, and the costs entailed from the collection of these duties by national authorities are more than compensated by the share that Member States retain (20%).
- » The largest part of the proceeds (80%) accrues directly to the EU budget and is not (in principle) accounted for as an expenditure item in national budgets. In the study commissioned by the European Parliament assessing how national budgets present information on own resources, only one Member State goes as far as considering proceeds from customs duties levies on their territory as a cost to the national budget instead of a receipt attributed to the EU.

In short, TOR are fiscal resources levied on companies and/or individuals, whose proceeds are attributed directly to the EU even if the collection is done at national level. This 'right of access to the source of taxation', which involves independence from decisions of Member States — also called financial autonomy —, is considered essential to qualify as an OR in the literature.

By contrast, national contributions which are used at supranational level to finance a common fund or a

common budget — or simply the costs of an institution — usually take different forms. They can be ad hoc donations or regular membership fees (as for many international organisations) or the contributions can be based on an agreed 'ex ante' key (percentages) as is the case for the European Development Fund, which is intergovernmental by origin.

*The VAT and GNI-based own resources are statistical aggregates which do not stem from an EU common policy.*

In the EU budget documents and in the annual Financial Report, the (statistical) VAT- and the GNI-based own resources are commonly summed up as 'national contributions'. Contrary to traditional own resources, these national contributions do not flow from a common policy. They arise from a statistical aggregate, such as GNI statistics used to calculate the GNI own resource. The measurement of the GNI basis is harmonised at EU level for own resources and other purposes, via the harmonised system of statistics and accounting (ESA), with detailed rules set out in binding legislation, and the annual figures are scrutinised by an Advisory Committee (comitology). This guarantees fair treatment and equity between Member States. In this sense, the GNI-based own resource is already an important step forward compared to other ad hoc contributions.

However, it does not create any link with an EU policy and the resulting amounts have to be carved out of the body of general income in national budgets. As a consequence, they have to be covered by Member States' general tax revenue and are thus [most often] treated as an expenditure item in national budgets, in competition with other spending items. This explains why Member States that are net contributors to the EU budget first look at their contribution on the revenue side — and try to minimise this amount as much as possible. The costs are immediately visible whereas the consequent benefits are often indirect and more dispersed.

For similar reasons, it is therefore not surprising that, from the beginning, the VAT-based own resource was considered a less 'genuine' own resource because it was simply a contribution from Member States calculated on the basis of a fiscal resource. As the VAT proceeds themselves first enter into national budgets, the VAT-based own resource does not imply a transfer of fiscal competence (like the TOR), but only an earmarking of a certain share of revenue ('affectation des recettes'). As explained above, this corresponds to how the GNI and VAT-based own resources are presented in the budgets

of the four Member States which recognise them as own resources.

These differences between the various components of revenue become manifest in the budgetary politics of annual and multiannual negotiations, as mentioned above in the case of the GNI-based own resource being perceived as a national transfers. In other words, some resources are considered less 'owned' by the EU than others.

### 1.2.3. Why is this important? Legitimacy and efficiency of EU decision-making

It is allegedly this type of revenue that the founding fathers had in mind when they formulated what is still the wording of Article 311 of the TFEU. And this is confirmed in the evolution of the sources of funding for the EU. Indeed, the EEC founding Treaty (the Treaty of Rome) made a clear distinction between a first phase which was to be financed through Member States' contributions (Article 200 EEC), and moving to a second phase where the Community budget would be financed through Community's own resources (Article 201 EEC).

There is a fundamental reason for this shift which can be traced back to the history of multi-level government structures in the 19th century: democratic legitimacy and more efficient decision-making.

*Own resources were designed to provide democratic legitimacy to the financing of the EU. They are ultimately decided by national parliaments.*

At the EU level, democratic legitimacy as an underlying objective can be inferred from the decision-making process concerning the two phases identified in the Treaty of Rome to fund the budget. Member States' contributions were decided by a Council decision only (at unanimity), while the own resources could be adopted, as they still are, only after the Council decision (still at unanimity) was adopted in all Member States 'in accordance with their respective constitutional requirements', that is to say, in general, with the agreement of national parliaments. The difference is very significant: it means that own resources 'imply a shift of sovereignty on the part of the Member states, allowing the Community to exert a direct power of taxation'. Such a shift, of course, can only be given by national parliaments.

The transition between these two phases allegedly occurred with the decision of 21 April 1970 'on the replacement of financial contribution from Member States by the Community' own resources'. This decision also led the Community to give budgetary powers to the European Parliament and to introduce direct elections for the European Parliament. However, with the gradual decrease in importance of the VAT-based own resource, and the continuous increase of the GNI-based own resource's share in EU financing since its introduction in 1988, we seem to be back to the situation pre-1970 (see Annex VI).

One argument often put forward in favour of such a system — more or less openly — relies on the assumption that national contributions allow Member States to control the size of the budget and impose budgetary discipline. However, the causality is not straightforward. Budgetary discipline is a fundamental principle of the EU budget and is enshrined in the Treaty, but it is first and foremost embodied in the fixing of the own resources ceiling, not in the composition of EU revenue. Budgetary discipline is further enforced by the fixing of expenditure ceilings in the multiannual financial framework, and in the annual setting of the amounts for authorised appropriations in the annual budgets or amending budgets.

Therefore, in an expenditure-driven, balanced budget, additional revenue from one specific source of revenue does not lead to higher spending levels, but to a different distribution between the various sources of revenue.

*RECOMMENDATION 2 – Budget neutrality. The structure of EU financing does not, as such, have an impact on the volume of the EU budget. The introduction of new own resources or other types of revenue would therefore — all other things being equal — result in reductions in GNI-based contributions, and could thereby create some margin of manoeuvre for national budgets or national fiscal policy.*

The Group considers that there are fundamental qualitative and political arguments in favour of changing the structure of own resources within the same volume. This is what is referred to generally as budget neutrality, which means that the support to new sources of revenue would not increase the EU budget but would simply reduce the 'national contributions'. Combined with a reform on the expenditure side, this

would help refocus budget negotiations on the quality of expenditure and rationale of EU policies, instead of being exclusively focused on net returns and on a vacuous zero-sum game which fuels the perception that some Member States are winners and other losers. It is therefore a false accusation to pretend that new own resources would increase expenditure at the EU level, because the latter is simply linked to another decision and not to the structure of the EU own resources.

Between what seems to be two extremes — a genuine own resource and a national contribution — there are other types of revenue sharing arrangements that are midway between the two. This type of revenue is often mislabelled 'EU tax', but is in fact a share of national taxes that Member States decide to transfer to the EU level, once there is a sufficiently harmonised approach concerning such taxes. Typically any variant of a VAT-based own resource follows this model, as would an own resource based on a financial transaction tax or on a carbon tax. Implementing Regulations at EU level can lay down the details of the harmonisation rules, the share or the amount of be attributed to the EU level, but all these own resources are based upon taxes existing or created at national level. The basic act of a tax can therefore be decided at EU level at unanimity, e.g. on the basis of Article 113 TFEU in the form of a directive such as for the Financial Transaction Tax. It is then transposed into national legislation, levied and collected by Member States. Whether its proceeds are used to finance the national or the EU budget is a separate decision (via the ORD). In such cases, the share of the tax attributed to the EU budget is a revenue sharing arrangement.

*Current own resources are not EU taxes. Taxes levied directly by the EU are not allowed under the current Treaty.*

In the light of the above clarifications, what would deserve to be called a real 'EU tax' would be decided and levied by the European Union, and the rates would be set by the EU legislative authority. The revenue would, a priori, accrue to the EU budget. As already mentioned, the Treaty does not allow this possibility and the EU would first have to be granted the power to levy taxes<sup>12</sup>. This is not a prospect that the present report considers realistic or even viable at present, and this is not what is proposed.

12. Certain measures of a fiscal nature are allowed for in the environmental and energy policy areas (Articles 192 and 194). See point 3.4.

### 1.2.4. Charting of the existing and potential own resources

On the basis of these considerations, a matrix can be drawn up with two axes in order to assess whether a given revenue source would be characterised as 'genuine':

The X-axis shows the various degrees of national and supranational decision-making and the (legal) nature of the fiscal arrangement: is the underlying legal act decided at national or EU level, at unanimity or qualified majority, with full involvement of the European Parliament or solely in the remit of the competence of national parliaments? On the one hand a purely national contribution based on an ad hoc key or ex ante percentage (such as the European Development Fund): on the other hand, an outright EU tax levied and collected centrally. The latter is presented for analytical purposes: as explained above, it would require enhanced EU competences and a Treaty change and are therefore not the Group's priority. In between, the various degrees of revenue sharing arrangements are presented.

The Y-axis represents the link to EU policies and competences. A revenue item can be entirely unrelated to EU policies and stem from Member States general tax funds (bottom of the axis). Or it can be connected with EU policies and legislation, such as the VAT Directive in order to ensure a harmonised basis. In such case, could it have regulatory co-benefits or dividends, or influence the behaviour of economic actors (with potential digressive effect on the level of revenue)? Alternatively, at the top of the axis, it can directly stem from an EU policy or competence (customs duties).

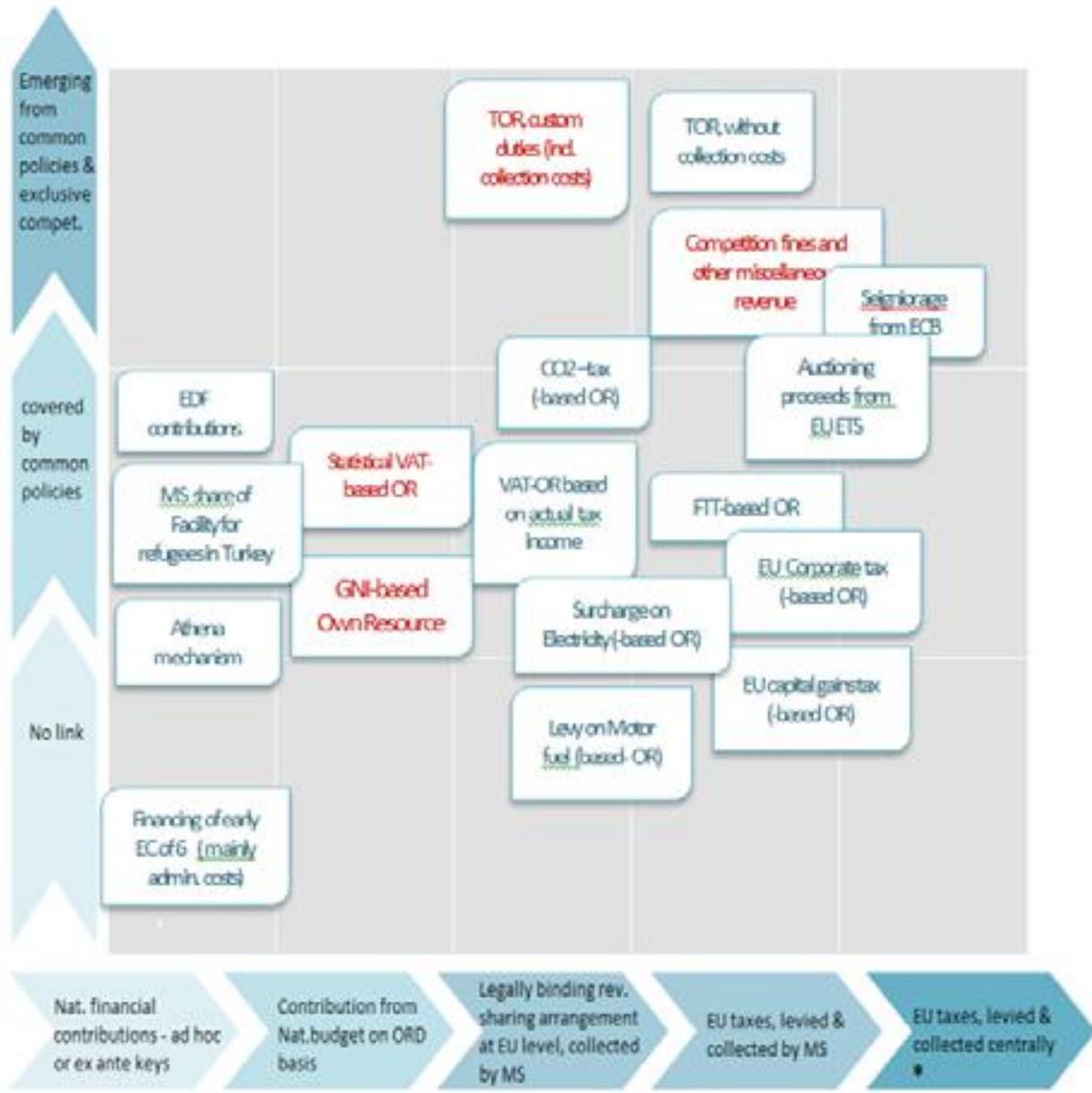
According to this matrix, revenue sources at the upper right would be more 'genuine', such as customs duties and revenue sources to the lower left would be more conventional contributions or transfers. Overall, the HLGOR considers that the objective of a future reform should be to finance the majority of EU expenditure via genuine own resources<sup>13</sup>.

Obviously, the positioning of many possible resources, like a real VAT-based or financial transaction tax (FTT)-based own resource would depend on the eventual design of the legal basis, its operational principles and implementation features. Similarly, an energy- or CO<sub>2</sub>-related levy can take many different forms. The table could therefore be further refined depending on the more precise characteristics of future proposals. Finally, the 'link to the citizen'-dimension is not easily incorporated into such matrix. Revenue accruing directly

to the EU budget without passing through national budgets or accounts would appear more genuine and might entail a higher visibility.

13. One member of the group thinks that own resources should focus on financing the EU budget while other EU policy objectives can be pursued via tax harmonisation without earmarking the revenue for the EU budget.

## Link to EU policies & EU competencies



## Legal nature, decision making modus (intergovernmental vs federal)

\* would require Treaty change

The depiction in this graph serves to illustrate the conceptual principles only. It does not imply that more ‘genuine’ revenue sources are per se more suited or desirable and it does not replace the qualitative and quantitative analysis in line with the criteria defined. Obviously, depending on certain assumptions or design features, e.g. central collection by an agency or collection by Member States, the location of any particular revenue source in this chart could shift.

### 1.3. Focus on European added value as a necessary precondition for a reform

The challenges identified in the introduction mostly concern areas which are not the most significant expenditure posts in the EU budget (in terms of volume). They also mostly coincide with areas where expectations from citizens are the highest as concerns EU policies. It is crucial to make the case for European added value in these areas to rebuild trust in the EU.

In the context of the mid-term review of the previous MFF, the European Commission provided a Staff Working Paper on 'the added value of the EU budget' which defines added value as 'the value resulting from an EU intervention which is additional to the value that would have been otherwise created by Member State action alone'.

This definition still holds, although there are many obstacles to using it as such to redefine budget priorities:

- » European added value is only partially measurable;
- » there are strong invested interests in the current policy and budget structure;
- » national preferences are divergent concerning these new areas of action.

#### 1.3.1. How to appraise European added value?

In order to make the concept of added value more workable, a useful distinction is to consider, on the one hand, added value before a common policy is envisaged or maintained and, on the other hand, added value after implementation.<sup>14</sup> The latter has been the focus of many efforts at EU level over the last decade, the latest being the Commission project 'EU focused on results', which is currently ongoing. However, the project focuses more on the micro-level and is therefore not the object of the present report. When conclusions can be made from this endeavour, they should become one important element of future decisions on expenditure, either to

evaluate the results and impact of a specific EU policy, or to measure positive side effects of EU interventions.

The former aspect of added value is already enshrined in the Treaty as one of the tools to test subsidiarity, even if this is not expressly mentioned. It refers to the classic notions of economies of scale, cross-national externalities and threshold effects (See some examples in the box below) which justify spending at the highest governance level, in accordance with the teachings of fiscal federalism. This macro-level approach to added value should allow us either to determine why spending at the EU level may be optimal compared to the national level, or to make choices between one EU policy relative to another.

Example of economies of scale: in some cases of public procurement it makes sense to 'pool and share'; in the area of defence research, a multiplicity of small scale activities may be less economically viable than one or a limited number of bigger projects.

Example of cross-border externalities: the Connecting Europe Facility (CEF) supports investments in crossborder infrastructure that national governments might not address unilaterally, because a share of the benefits would accrue to the citizens and users on the other side of a border. Similarly, soil, air or water pollution can have negative externalities which justify common action or regulation. If this is not the case, free rider behaviour is encouraged and costly consequences are endorsed by the entire society, rather than the polluter.

Example of a threshold effect: large scale projects like ITER or Galileo depend on sizeable investments which cannot be made by a Member State alone. They also rely on shared research and technological know-how.

Economists have tried to measure European added value in specific areas and have come up with very variable conclusions<sup>15</sup>. However, there is a consistent criticism towards the two major spending posts — agriculture and cohesion — as being essentially redistributive and not providing enough added value, partly because Member States focus their efforts to 'get their money back', and partly because policies are not optimal.

14. This distinction is a simplified version of the matrix developed by researcher Eulalia Rubio in 2011, Notre Europe — Jacques Delors Institute.

15. The European Added Value of EU spending: can the EU help its Member States to save money? Exploratory study by Bertelsmann Stiftung, 2013. The study analyses three cases in details and concludes that added value:

- cannot be proved in the case of the CAP (which, despite high EU spending, still requires substantial spending at national level);
- is clearly proved if national embassies of the 28 Member States in third countries were to be replaced by EU embassies;
- can be proved in the case of the integration of European land forces (EU army) depending on the decisions to be made relating to the size of the forces and their administrative regime.

*EU policies with the potential highest added value are currently the most modest in budgetary terms. The added value also depends on Member States' decisions to actually make use of potential cost savings.*

On the other side of the argument, two areas seem to be consensually identified as having a high potential added value: research and development, and internal and external security. Research and development is already an important element of EU spending, although research suggests that there is a worrying trend in favouring applied research, where immediate or short-term results can be used in industrial applications, rather than fundamental research, which requires a long-term vision and patience in relation to immediate economic benefits, but is the highest segment providing added value. Beyond this inherent problem of research policy, the fact remains that EU research and development accounts for a much more modest share of the EU budget than agriculture and cohesion policies.<sup>16</sup> In a global context where EU research is compared to American, Indian or Chinese research, this should be one of the essential policy priorities in the future.

Internal and external security has emerged as the foremost area of European added value in recent years, due to the pressure of the migration crisis, which has put into evidence the dire gaps in the Schengen zone, and to the new terror threats which concern most if not all Member States.

Internal and external security should be the main focus of the EU in the coming decades for many reasons: peace is at the heart of European construction and, while this has been its greatest achievement by ensuring that traditional armed conflicts between Member States would no longer be possible, this greatest achievement is being jeopardised by new security threats — both internal and external — which are perceived as the greatest challenge to peace on the European continent.

Assessing the European added value of internal and external security would depend on the precise scenarios envisaged and whether they require cooperation, joint actions, or common and integrated actions. There has been increasing cooperation in these areas, notably common policy regarding visas, asylum, and consular cooperation, but the pace is slow. The Schengen agreement was signed in 1985 by 6 of the then 10 Member States of the European Community. It now counts 26 Members (the UK and Ireland have not signed the agreement). The objective of the Schengen agreement was to create a single area without internal

border checks — from which citizens have benefited since 1995.

But running counter to the opening of all internal borders, is the fact that is a common policy on external border management, has taken much longer to be addressed, and with a lot of reluctance. However, migratory pressures have caused the acceleration of the establishment of common standards for controls at the external borders, the gradual implementation of an integrated system for the managing of those borders, and the creation and then reinforcement of Frontex, the European agency in charge of this policy.

*Some EU policies with the potentially highest added value also coincide with areas at the conventional core of nation-states' sovereignty, such as internal and external security.*

This state of affairs is not surprising: internal security is perceived as one the last governing functions of nation-states whose implementation at national level seemed, at least until recently, adequate and efficient to ensure sovereignty. It only emerged as a European public good once intervention at European level became perceived as necessary while action at national level has become insufficient to counter threats and criminality that ignore borders.

External security is an even more complex matter. In regular European Barometer polls, citizens show a massive and consistent support for a common European defence (reaching in most cases 80% of favourable opinion, and in the most sceptic countries, over 50%). It is one of the few areas for which there is a kind of innate sense among Europeans that the global challenges for their security cannot be met and won with the traditional means at the disposal of nations. This therefore seems to be a natural European public good, for which European added value should be easy to demonstrate.

But as is the case for internal security, the test of added value to determine whether spending at the EU level may be optimal compared to the national level is not only appraised in economic terms. It requires political consensus, and only then can it be reflected in major initiatives or spending reallocation.

This can be observed in the evolution of some EU budget priorities over the last two years. While Heading 3 'Security and Citizenship' as adopted for the period 2014-2020 was the smallest spending priority of the period, it benefited from the highest increases: in the

2016 EU budget, it was topped up significantly to EUR 4.05 billion (from EUR 2.52 billion in 2015), with the amounts above the ceiling covered by the flexibility instrument. Additional funding was allocated mainly for the AMIF (Asylum, Migration and Integration Fund) and for the Internal Security Fund; in the draft budget for 2017 as presented by the Commission, migration remains one of the priorities in the EU budget.

Another interesting feature is the proposed preparatory action for defence and security cooperation and research, although with a very modest amount of EUR 25 million in 2017. It will cover defence research projects, technology and development activities, and could be a signal of future changes in EU priorities if defence spending at EU level is initiated.

*Under the current Treaty, the EU budget cannot finance actions with military or defence implications.*

It should be underlined at this stage, though, that the Lisbon Treaty prohibits the EU budget from financing actions or measures with ‘military or defence implications’. This legal restriction is reflected in the ‘different keys’, or burden-sharing arrangements, that apply to such actions and that are financed outside the EU budget. Any significant reorientation of EU budget priorities to include military costs could therefore only be a remote perspective necessitating Treaty changes. For the purpose of the present report, which aims at presenting funding solutions within the current Treaty, the European financing of defence could only be decided through ad hoc means outside the EU budget.

The two examples above, research and internal and external security, concern two areas where the merit of action at the EU level is already established, or is justified in economic, political and social terms. However, this does not necessarily translate into EU spending priorities, in particular in current times of rarefied public resources which are squeezed in an ever growing dilemma of having to finance more with less.

For this dilemma to be addressed, it is not enough to consider European added value as an absolute but also as a relative notion, in order to identify among the areas providing European added value those which generate the highest value. This exercise, like the previous one, is not only an economic test. It involves political judgement about the relevance of public action in different domains and ultimately varies according to national preferences, and can even reflect the confrontation of different visions of the EU project.

This relative appraisal of the different EU spending areas one to another is particularly helpful for the reform of own resources because it would identify — in a fixed and limited EU budget of about the same size of the current one — which EU policies provide the highest added value content. If the EU budget is used to finance these as a priority, it would then no longer be seen as a zero-sum game between Member States, or less so at least. The EU budget would finance actions that benefit all.

*The added value of EU policies is not static and can be improved over time.*

In this context, there are two important elements which should be taken into account when assessing the added value of current EU policies: the first is that successive EU budget reforms have already increased the EU added value, at least partially, or should increase it further in the coming years (the implementation of the 2014-2020 cohesion programmes has started at a slow pace and their performance will have to be judged in the coming years); the second concerns the new financial instruments, whose economic importance is on a continuous upward trend. These two aspects have been examined in details in the external study commissioned for the HLGOR and essentially highlight that the European ‘quality’ of EU spending has increased over the years without being reflected or recognised as mutual benefits.

### **1.3.2. Two recent developments which increase the European added value of EU expenditure?**

#### **1.3.2.1. A gradual shift from local to EU objectives**

*A more systematic appraisal of the cross-border effects and second-level benefits of EU policies should be undertaken.*

1. The first aspect — the increased added value of existing European policies — is far from being consensual among economists and would therefore require additional analysis. Available studies have most often been based upon partial data which makes it difficult to build a comprehensive view that would take into account, for example, ‘second-level benefits’ and

positive, cross-border external effects of EU policies. As a result, the argument is often reduced to providing examples of projects which are judged as having no European value at all, against projects which show clear cross-border positive effects or benefit more than one recipient.

As Heinemann (2015) points out, the EU budget is still financing too many projects with questionable EU added value. Some of these may well be 'compatible' with the thematic objectives or other EU objectives. This is partially due to path dependency. Cohesion Policy, like the CAP, was originally developed in response to a number of national requests. The policies responded to local needs, and not necessarily to EU-level objectives. The goal of regional convergence was perfectly compatible with investments focusing on local benefits without a link to a wider EU objective. The need to link investment to 'European' policy objectives is recent. The EU budget was also used to 'compensate' for the some negative impacts on specific groups in society. As a consequence, for many years some projects have been 'permissible', while being questionable from the point of view of their European added value.

*The EU budget is still financing too many projects with questionable EU added value.*

In particular, ESIF spending in infrastructure or measures in the tourism sector with predominantly national or even local added value in more developed regions in the richer Member States is in the crossfire of criticism. Why should the European taxpayer have to pay for such redistributive operations? Does this not diminish, rather than add value?

This is a key economic criticism to a certain category of EU spending. As long as a large part of the EU budget is dedicated to projects perceived as having only local value, with no cross-border or EU-wide benefits, Member States will continue to put a lot of emphasis on net balances, with budget negotiations be perceived as a zero sum game and dominated by distributional conflicts. In short, Member States will pursue their efforts to 'get their money back' and press for EU spending on projects within their own borders because EU financing or co-financing of projects generates a direct financial benefit to them.

*The financing of policies which would benefit all EU citizens and finance public goods (such as internal and external security, the fight against climate change, etc.) is not 'attractive' today because of the way each Member State accounts for the 'benefits' it gets from the EU budget.*

In contrast, the benefits of spending on EU-wide public goods are spread across all Member States. For each individual Member State, supporting this type of spending today appears less attractive. If the decision-making process regarding the structure of spending could be changed so that spending on EU-wide public goods dominates the budget, there is hope that the focus on net balances would be crowded back. Or, if the EU-wide or cross-border benefits of EU policies were accounted for in — or next to — net balance calculations, they would provide a more accurate picture of the impact of EU policies (see point 3.1.). Ways forward to reduce the bias of spending on projects reflecting narrow national self-interest of individual member states would be to increase the co-financing in regional and structural policies, and to finance the CAP differently, for example through a cohesion-based system of direct payments, as argued in the external study commissioned by the Group.<sup>18</sup>

*Traditional EU policies like regional policy provide more added value today thanks to the definition of EU-wide objectives.*

2. Some researchers, on the other side of the argument argue that the nature of EU expenditures in Member States has radically changed since the 1980s, and that this is not reflected in the net balances. The Cohesion, Structural and Rural Development Funds have increasingly become instruments to achieve EU objectives (Europe 2020 objectives for example) in important areas, such as energy and transport, environmental protection and innovation, with a minimum reallocation of funds to these objectives. And, as they point out, many of the environmental and energy objectives of the EU have been designed and led by countries with high standards, which tend to be the largest contributors to the EU budget. This should not be a surprise: the same process happened, in the 1980s for example, when the EU environment policy took off, pushed by the more conscious, and often richer, Member States.

<sup>18</sup>. See footnote 2. Ibid. pp. 129-133.

This process has reached new heights with the creation of the 11 thematic objectives<sup>19</sup> and complex, strategic planning requirements under the new 2014-2020 structural programmes. These requirements, some of which started with the previous MFF, are not negligible and represent a strong departure from the past. They entailed a complete rethinking of cohesion policy so that the development of the economies of poorer Member States is seen as bringing benefits to the Union as a whole, and more than just financially: they also generate political stability, reduce social tensions and internal migration.

In short, EU regional and rural development funding is being used to achieve common objectives, such as reducing greenhouse gas emissions and attaining high levels of environmental protection. As EU standards are often more stringent than what countries with a lower level of GDP would have adopted on their own, the EU budget is de facto partially compensating them.

*EU expenditure provides additional growth in all Member States, while this effect is not visible in the accounting calculation of net balances.*

3. Another interesting approach is the attempt to estimate the change in the demand for goods and services generated by EU expenditure. The starting assumption is that each euro spent from the EU budget gives rise to an increase in production, which can then be divided among the different sectors of the economy: agriculture, industry, services, etc. In the report for the Commission on own resources in 2005, Le Cacheux showed that EU expenditures provide additional growth for all Member States, including net contributors. The real burden of a budgetary transfer and the real benefit triggered by EU expenditure are therefore different from the simple accounting approach used to calculate net balances.

Recent studies reinforce this position. Evaluations of the Cohesion Policy over the 2007–2013 period estimate

that this policy achieved a substantial contribution to growth and jobs, with larger long-run effects. Many tools have been used: quantitative information, evaluation of particular programmes or interventions, econometric techniques and counterfactual impact evaluation with, for example, macro models that simulate how the economy would have evolved in the absence of the policy and compare the potential situation with the way it actually developed. In a recent report for the European Parliament (Núñez Ferrer and Katarivas, 2014), a review of these show that the EU budget has considerable impact on the EU Member States' economies and on the EU as a whole.

The results of these studies, so far, have not influenced the political process, which does not take into account secondary or cross-border effects, or EU-wide benefits. However, the consistent request, over the years, to focus on EU added value is a recognition that there is some expenditure worth undertaking regardless of their location: the reduction of emissions, for example, can lead to financing cleaner power stations or cleaner transport in cities. They benefit directly the citizens living close to these power stations or in these cities; but they also benefit all as part of the common EU policies to protect the environment and fight against climate change. However, such interventions, which provide EU added value, are not perceived or accounted as such, in today's accounting approach of the costs and benefits of EU membership.

### 1.3.2.2. The increased use of financial instruments

1. The second aspect increasing the added-value of EU expenditure concerns one of its delivery mode: the increased use of financial instruments. Financial instruments provide financial support from the EU budget to final recipients through loans, guarantees and equity investments.

Most financial instruments are (correctly) not pre-allocated geographically, and the financial flows

19. Thematic objectives under Article 9 of the Common Provision Regulation (EU) No 1303/2013 for the European Structural and Investment Funds (ESIF):

1. Strengthening research, technological development and innovation;
2. Enhancing access to, and use and quality of ICT;
3. Enhancing the competitiveness of small and medium-sized enterprises, the agricultural sector (for the EAFRD) and the fisheries and aquaculture sector (for the European Maritime and Fisheries Fund);
4. Supporting the shift towards a low-carbon economy in all sectors;
5. Promoting climate change adaptation, risk prevention and management;
6. Protecting the environment and promoting resource efficiency;
7. Promoting sustainable transport and removing bottlenecks in key network infrastructures;
8. Promoting employment and supporting labour mobility;
9. Promoting social inclusion and combating poverty;
10. Investing in education, skills & lifelong learning; and
11. Enhancing institutional capacity building & efficient public administrations.

generated vary from project to project and depend on the nature of the investments. Economists generally acknowledge that the return on investments of additional infrastructure declines for a given level of GDP, and that the latest disinvestments in infrastructure seem to have affected growth potential more often than not in the wealthier Member States, where the capital-to-GDP ratio has fallen. The situation is usually reversed in research and development, where the returns on investment and attraction of capital are usually higher in advanced economies. This is also the case for investment in small and medium-sized enterprises (SMEs), because there is a stronger demand-side stimulus in countries in better economic condition.

Interestingly, the external study commissioned by the Group shows that the distribution of financial flows resulting from the main financial instruments diverges from the traditional distribution of co-financed Cohesion Policy grants, agricultural subsidies or even Research and development grants. It confirms the comparative advantage of wealthier Member States in attracting this kind of funding.

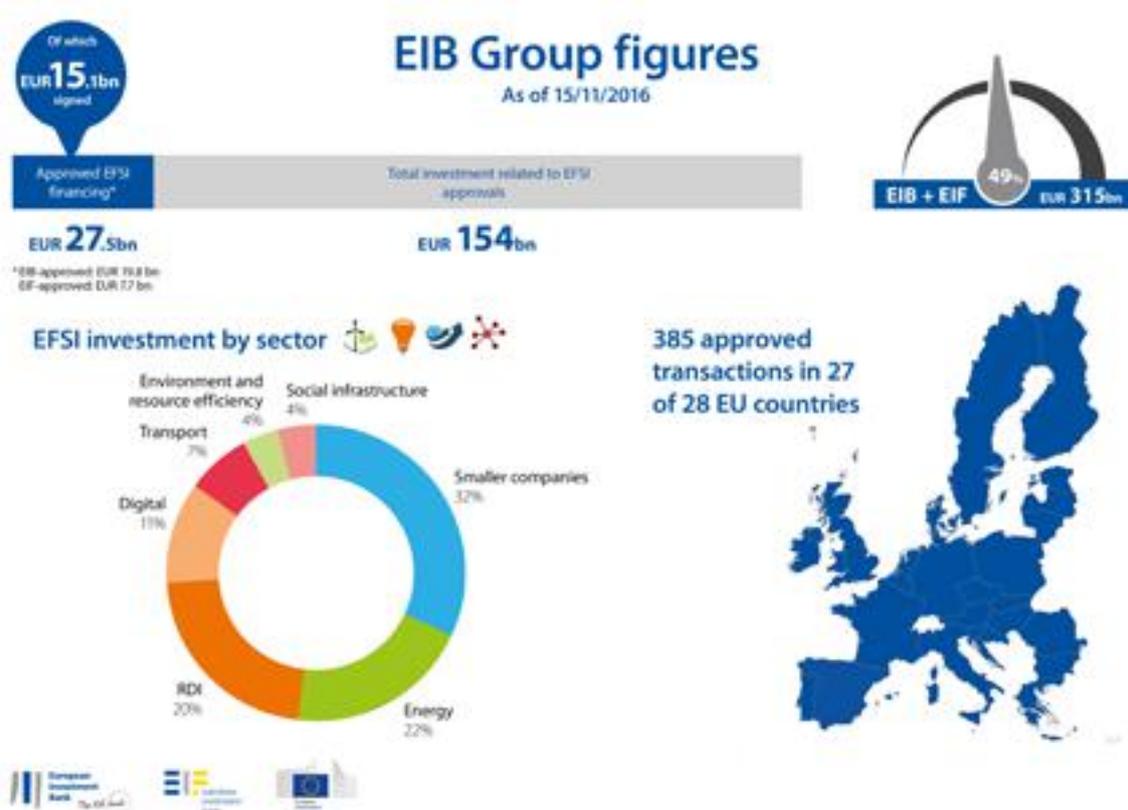
*The distribution of the main financial instruments in Member States is different from traditional EU policies, notably agriculture and cohesion.*

The budgetary impact might seem modest today in relation with the whole EU budget, but compared to grants, financial instruments have two advantages: they leverage additional private and public funds; their capital endowment is of a revolving nature, as the same funds are used in several cycles.

2. On 26 November 2014, the Commission presented the European fund for strategic investments (EFSI-I). The EFSI is a EUR 16 billion guarantee from the EU budget, complemented by a EUR 5 billion allocation of the EIB's own capital with the objective of mobilising at least EUR 315 billion in additional investments by mid-2018 (with a leverage of 1:15). This amount rivals the size of the whole Cohesion Policy for the period 2014-2020.

At the latest reporting in November 2016, projects and agreements have been approved for EUR 27.5 billion, committing EUR 154 billion in investments across 27 Member States; almost half of the investments initially foreseen has been achieved. With more than one third of total investments the absorption has been particularly relevant under the Small and Medium-sized Enterprises (SME) window.

On the occasion of President Juncker's 2016 State of the Union address, the Commission proposed to extend and to reinforce the EFSI (EFSI II): this would bring the period to 2020; the EU guarantee is increased to EUR



26 billion and the EIB capital to EUR 7.5 billion, which should mobilise private and public investment of EUR 500 billion over the period until 2020.

The EFSI delivers support with no geographic or sector quotas and additionality is a fundamental feature: support is pointed to market failure or suboptimal investment situations. In this sense, EFSI provides funding for economically viable projects where it adds value, and including projects with a high risk profile.

The accountability set-up of the EFSI seems focused, so far, on outputs rather than outcomes and impacts.<sup>20</sup> Therefore, it is still difficult to evaluate the financial flow across countries and the value added created. As for first results, geographic distribution seems to show that investments are concentrated in wealthier countries, and in particular in net contributors' countries, and in the SME sector. This situation can lead to cases where the allocation of funding at this stage is concentrated in countries with the least amount of SME-financing difficulties, such as Germany.

This is not a criticism of the existence of the EFSI, which has proved an extremely dynamic tool to guarantee and mobilise private investment in line with the

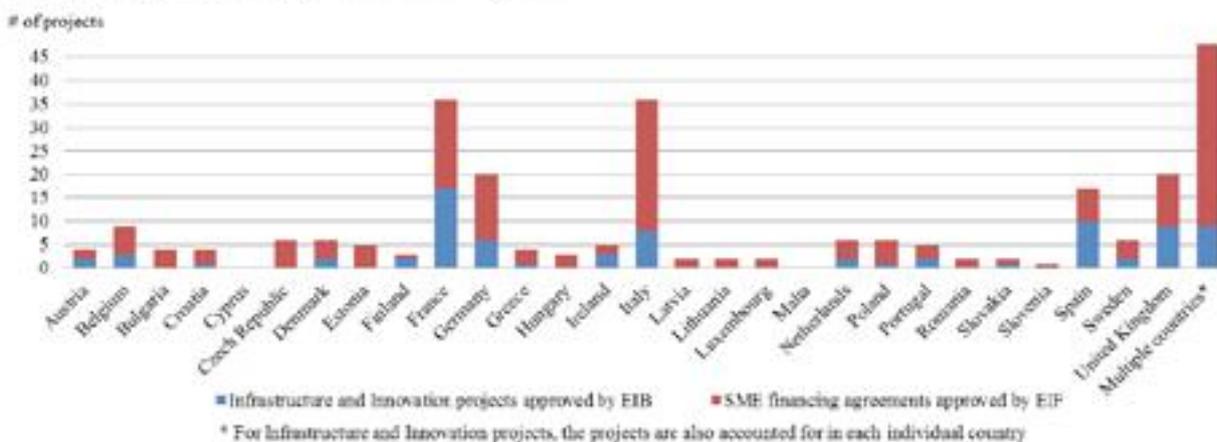
change over time. Investments go to where the economic environment is reassuring for investors, which may change.

It is rather an observation that EU financial instruments generate large flows of investment, which are not captured by the net balances. This should therefore prompt the question of who benefits from the EU budget today, and who is likely to benefit in the future with the expansion of centrally managed headings and financial instruments. Is it those who receive more transfers, or those who mobilise the most funding from support triggered by the EU budget?

*The effects of the financial flows triggered by EFSI and other financial instruments are not captured by the net balance calculations.*

3. The experience of the EFSI is reflected in other centrally managed funds, such as the Project Bond Initiative, the Loan Guarantee Instrument for trans-European Transport Networks, the European Energy Efficiency Funds and the Marguerite Fund.

**EFSI geographic coverage - as of end-May 2016**



Source: European Commission<sup>21</sup>.

Europe 2020 objectives. EFSI is primarily designed to address suboptimal investment situations and even if it has introduced limits to sectoral and geographical concentration, its role is not redistributive. In addition, as the capacity to use financial instruments increases in cohesion countries, the geographical impact might

As for financial instruments which support research and development, the numbers speak for themselves as well. Under the previous Seventh Framework (FP7) and Horizon 2020 programmes, the EU budget supported the European Investment Bank in lending and further leveraging funds for innovative projects. The risk-sharing

20. ECA Opinion No 11/2015 concerning the proposal for a Regulation of the European Parliament and of the Council on the European Fund for Strategic Investments – April 2016.  
 21. COM(2016) 359 final, "Europe investing again. Taking stock of the Investment Plan for Europe and next steps", Communication from the Commission to the European Parliament, the European Council,

finance facility (RSFF) and risk-sharing instrument (RSI) raised over EUR 10 billion. As from 2014, the follower programme (InnovFin — EU finance for innovators) additionally raised over EUR 1 billion. Special guarantee, loan and venture capital instruments have been created to help SMEs and mid-caps to access funds. The geographical distribution of the RSFF, while covering 23 countries according to the second interim evaluation of 2013, has 48% of the funding concentrated in France, Germany and Spain.

These findings confirm that wealthier Member States have a comparative advantage in attracting funding for R&D and innovation, as was reflected in the distribution of the FP7 funds disbursed from 2007 to June 2014: 13 countries received 95% of the FP7 funding. Among them, Germany, the UK, France, Belgium, Spain, Italy and the Netherlands got the biggest share. If we look at the per capita distribution, the Netherlands, Denmark, Sweden, Finland and Belgium dominate the ranking.

*Research investment provides important economic returns and added value in the business sector.*

4. The economic returns of research investment are particularly important to consider because they are a key driver for growth. Using an OECD model developed by Guellec and Van Pottelsberghe (2004), the Joint Research Centre estimated the effects of the Sixth and Seventh Framework Programmes on the growth of total factor productivity of the EU and associate countries. The results show that on average, for every euro invested by the EU research programme, EUR 13 was generated in increased added value in the business sector. The impact depended on the structure of the country, the market size and the industry structure, which suggests that benefits are likely higher in the most advanced countries with the largest markets.

A look at the EU industry R&D scoreboard also confirms the same geographical concentration of Europe's leading companies in terms of investment in innovation (which invested more than EUR 15.5 million in R&D in 2013) in the areas with the highest potential returns.

'It is important to reiterate that this report does not judge the distribution of spending as negative. What this report does judge is the erroneous position of some Member States that consider that they do not benefit from contributing to the EU budget, based solely on the public fund flows.'<sup>23</sup>

5. While the financial instruments referred to above are not geographically pre-allocated, some financial instruments are embedded in structural policies, and thus pre-allocated. They are meant to expand under the new cohesion programmes.

The performance of these instruments is generally positively affected by the quality of the institutional set up and administrative capacity, such as in Poland, Estonia and Germany, and negatively affected by unexpected regulatory barriers, or the lack of quality projects which leads to funds being stranded in non-performing funds. There is a high risk for decommitment of such funds in 2017, as well as for complex funds such as urban funds. The Court of Auditors' annual report for 2014 and the European Commission's replies stated that 'the financial instruments in Bulgaria, Greece, Spain, Romania and Slovakia were severely hit by the economic and financial crisis' (op. cit., 6.49). Financial instruments are not tools that can be deployed successfully in all economic circumstances.

*By the end of the current MFF, the financial flows stemming from all financial instruments combined could rival the size of the EU budget.*

6. This short review of the leverage and multiplier effects of the EU budget in recent years shows how the financial flows are increasing in importance and follow different distribution patterns than traditional EU expenditure. Financial instruments and an increase in research and development spending are the main reasons for these shifts.

This development is important because the total investment flows stemming from all financial instruments combined could rival the whole budget by the end of the 2014-2020 MFF. At the minimum, it shows that such funding considerably departs from the current zero-sum game at the heart of the calculation of net balances.

### **1.3.3. A more comprehensive approach to assessing added value**

While it is not the main objective of the present report to provide a comprehensive review of European added value, it considers it essential for the EU to reflect more

23. See footnote 2. Ibid. pp. 45.

accurately the real impacts of EU policies, whether to integrate the mutual benefits in their assessment or criticise their absence.

The present chapter tries to shed some light on recent developments which affect the European added value of EU funding. The increased focus on EU objectives rather than the simple choices of beneficiary countries will certainly be difficult to measure, but they could at least be explained and made more visible. What is clear however, is that hundreds of billions of financial flows facilitated in part by the EU budget are nowhere accounted for in the present perception of the costs and benefits, as will be demonstrated in point 3.1., and this makes the exclusive use of net balances as an indicator to identify 'excessive net contributors' not only misleading, but also senseless.

*RECOMMENDATION 2 – European added value. In times of scarce public resources but growing financial needs, the EU budget needs to focus on areas bringing the highest 'European added value', or on European public goods for which action at EU level is not only relevant, but indispensable, or where national financing possibilities are insufficient for achieving our European goals.*

## PART 2 — BUILDING BLOCKS OF A ROOT AND BRANCH REFORM

### 2.1. A new rationale for own resources?

The current system of own resources is mostly focused on providing stability and sufficiency of revenue, and equity between Member States. Previous reforms have been mostly negotiated with the last concern at its centre, i.e. equity between Member States.

While fairness needs to remain central for any reform to be successful, in particular given the decision-making procedure which requires unanimous agreement, some additional concerns have been neglected in the past and should also guide decision makers. The mandate of the Group clearly underlined the need to pay particular attention to four criteria in order to assess the suitability of future sources of revenue: '4. The Group will undertake a general review of the Own Resources system guided by the overall objectives of simplicity, transparency, equity and democratic accountability.'

In its First Assessment Report, the Group identified five general criteria and three EU-specific criteria which should guide a thorough and meaningful reform. It also highlighted that some criteria were interpreted in various ways depending on value judgements and opinions expressed during negotiations, in particular the criterion of fairness.

Discussions since the release of the First Assessment Report have confirmed that all these criteria remain valid today. They have also reinforced the view that some of these criteria could be contradictory and are more helpful if the own resources system is assessed in its entirety rather than through individual resource. No single resource would fulfil them all (see Annex VII).

*A reformed system of own resources should lead to a more sustainable financing of the EU in terms of environmental, social, economic growth and good governance objectives.*

One encompassing concept has also emerged from recent academic sources: the implications for sustainable development of the own resources which would compose the funding of the EU budget in the medium to long term. Sustainability encompasses several dimensions: environmental, social, economic

growth and good governance. The rationale behind this concept is twofold:

- » the current system of EU own resources does not contribute to the central EU objectives of 'smart, sustainable, inclusive growth' as laid down in the Europe 2020 strategy, or to the sustainable development goals;
- » sustainability-oriented tax-based own resources may reduce or compensate for the sustainability gaps in EU Member States' tax regimes.

The absence of any fiscal or policy co-benefits might give rise to opportunity costs. Should new own resources be introduced according to this rationale, they could have positive effects or side effects such as correcting negative externalities or market/government failures and thus bringing benefits other than simply financing the EU budget, as explained in the previous chapter. The resulting own resources system would generally be more geared towards providing European added value than it currently is.

Sustainability is captured in all its economic, social, environmental, cultural and institutional dimensions, and in fact covers most of the criteria already identified by the group. At the same time it also provides a new and interesting narrative:

- » in its economic dimension, it concerns economic growth, fiscal sustainability, and economic welfare;
- » its social dimension covers social sustainability; employment, social inclusion, cohesion and mobility, and wellbeing and quality of life;
- » its environmental dimension covers the fight against air pollution, green innovation and renewable energy;
- » finally, its cultural and institutional dimensions covers horizontal tax harmonisation, tax non-interference and fair distribution of the financial burden across Member States.

*Own resources can be designed to help address the sustainability gaps of the internal market.*

Taking into account these various elements, considerable sustainability gaps in taxation in the EU can be identified: the high and increasing weight of labour taxes, the decreasing weight of corrective (particularly environmental) taxes, intense company tax competition including profit shifting of multinational corporations, issues of tax compliance and tax fraud, and a decrease of (perceived) fairness of EU tax regimes. This corresponds to the arguments put forward by the European Commission in a recent Communication to re-launch the common consolidated corporate tax base (CCCTB).

Tax-based own resources if designed accordingly may be suitable instruments to reduce these sustainability gaps and to preserve the sustainability of EU integration, by contributing to central EU objectives, as anchored in the EU 2020 strategy or the sustainable development goals. For example, environmental taxes like a flight ticket tax, or revenues from a CC(C)TB-based corporate income tax, are increasingly difficult to enforce at national level for fear of creating competitive disadvantages for the national economy. At the EU level, however, such taxes can directly strengthen the sustainability of taxation in the EU, for example by improving environmental effectiveness or perceived fairness of taxation. In addition, and more indirectly, by allowing Member States to decrease their GNI-based contributions to the EU, tax-based own resources would create leeway for Member States to decrease national taxes less conducive to sustainability, in particular the high taxes on labour.

Ultimately, the choice lies with Member States who are alone have the power to decide on fiscal matters, but a different and more sustainable system of own resources based on taxes can create the conditions for Member States to make such a choice. This is what added value of the revenue side of the EU budget could bring. Maintaining the current system would only be conducive to the same pursuit of tax competition between Member States, aggravating the race to the bottom concerning corporate tax in particular.

*RECOMMENDATION 2 - Own resources should not only be used to finance the EU budget in a sufficient, stable and fair manner. They should also be designed to support EU policies in key areas of EU competence: strengthening the Single Market, environmental protection and climate action, energy union, and reducing the fiscal heterogeneity in the Single Market*

## 2.2. Own resources examined by the Group

In the following chapter, each own resource — 'genuine' or not — is examined in relation with the various criteria reiterated above, in order to identify its strengths and weaknesses. This should be conducive to proposing an optimal role for these resources within a larger basket of own resources or global expenditure/revenue package (see Part 3).

### 2.2.1. Current own resources which the Group considers should be maintained

#### 2.2.1.1. The GNI-based own resource

Since 1988, GNP/GNI-based contributions constitute own resources and have become the keystone of the own resources system for financing the EU budget, given that it provides the revenue required so that the EU budget is always in balance. In practice, the GNI-based OR is calculated as follows: first, the revenues yielded by the traditional own resources and the VAT-based own resources are established on the basis of the forecasts given by the Member States, and jointly endorsed; second, the amount of the adopted budget which remains to be covered is calculated; finally, that amount is split into national contributions resulting from the application of a call rate to Member States' GNP/GNI bases.

#### How does it score in relation with the criteria?

**1. Equity/Fairness:** the GNI-based own resource is perceived as equitable and fair in the sense that it respects the ability to pay of Member States: countries with the highest GNI, and therefore the strongest economies, usually contribute more to the EU budget. This picture is however nuanced once the corrections are taken into account:

- » the United Kingdom contributes significantly less than its share in the EU GNI (10.70% against 14.75% on average for the period 2007-2013);
- » to varying degrees, Germany, the Netherlands and Sweden contribute proportionally less than their share of EU GNI (from a fraction of a percentage for Sweden to almost 1% less for the Netherlands and Germany);

- » almost all other Member States, as a result, contribute more than their GNI share, from a fraction of a percentage to almost 2% more.<sup>26</sup>

Moreover, if equity is estimated at the level of citizens, the present system of 'national contributions' then appears as 'regressive': Member States with a lower GNI per capita do not contribute a lower share of 'national contributions' expressed as a percentage of their GNI. The redistributive effect between Member States and between taxpayers is therefore less clear and, in any case, only indirect.

**2. Efficiency:** the GNI contributions are paid on the first working day of each month, usually at the rate of one-twelfth of the annual amount. The current system has proved very efficient, as high interest on late payments has ensured that payments are usually made on time. The calculation of the contributions stem from the figures provided from the national and European statistical authorities, which are discussed with the Commission annually in the Advisory Committee on Own Resources. Once the GNI data are final, it is annually communicated to the GNI Committee, which formally provides the figures to the Commission for the adjustments to the GNI contribution of each individual Member State. This exercise provides a clear and fair procedure.

**3. Sufficiency and Stability:** as the residual or balancing resource, the GNI-based own resource, is instrumental in providing stability and sufficiency to the revenue of the EU budget, annually and in the medium term, within the overall ceiling for the total amount of own resources that may be collected for the EU budget (1.23% of EU GNI). By definition, the stability it provides for the whole system is ensured by its own flexibility and regular adjustments in the course of budget execution: it therefore remains something of a moving target which can create difficulties during annual budget negotiations, both at EU and national levels. It is also by definition sufficient, as it is not linked to a particular source or tax but draws on the general budget revenue of Member States. On average, the share of GNI own resource in total own resources reached around 75% over the last 5 years. In the EU budget 2017 the actual amount estimated to be received amounts to around EUR 94 billion or 71% of the total own resources.

**4. Transparency and Simplicity:** GNI-based contributions are in theory simple, based on the share of each Member State in the total EU GNI. However, the introduction of many corrections or reductions for some Member States<sup>27</sup> has led to increased divergence between the share of some Member States in the total EU GNI, and the share of these same Member States in the total of contributions which finance the EU budget. Transparency is hindered by the fact that GNI-based contributions are treated very differently in national budgets (see point 1.2.1.2.), appearing in most cases as expenditure instead of earmarked revenue, and might thus be perceived as being conditional on the vote on national budgets. This is a misrepresentation of what own resources are, even if it does not have legal implications because the transfer is automatic.

**5. Democratic accountability and budgetary discipline:** the GNI-based own resource is often presented by net contributors as a tool to enforce budgetary discipline because it is perceived as a budgetary transfer on which treasuries are supposed to have more control. In reality, GNI contributions are transferred automatically, in accordance with the Own Resources Decision (ORD). However, they have nonetheless contributed to increasing the political pressure to reduce the EU budget and the MFF over the last two decades, at the level of both national and European annual budgets. In this context, how these 'national contributions' are presented in national budget certainly plays a role. As concerns democratic accountability, the underlying data on which the GNI statistics are built does not generally go through parliamentary scrutiny in Member States but is under the responsibility of national statistical offices.

**6. Focus on European added value:** there is no link between the GNI-based own resource and EU policies. Experience shows that these contributions are the focus of national interests in multiannual budgetary negotiations.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** the GNI-based own resource is by definition not a tax and does not impact on the fiscal preferences of Member States. As regards subsidiarity, while the same GNI calculation rules apply to each Member State, the underlying data are produced

26. 'Financing the EU budget — Moving forward or backwards?', Gabriele Cipriani, 2014, p.20. See Table 6.

27. To mitigate what has been called since the Fontainebleau Declaration 'excessive imbalances of net contributions', several corrections have been introduced, usually in the form of lump sums. The most famous one is the UK rebate. Some countries have obtained a 'rebate on the rebate' for financing the UK rebate and finance together around 10% only of it. The Member States concerned are Germany, followed by the Netherlands, Austria and Sweden. Most of the UK rebate financing rests on the other Member States, notably France and Italy which finance almost 50% of it. In addition, under the new Own Resources Decision of 2014, and for the period 2014-2020, temporary reductions in the GNI contributions have been agreed for the Netherlands (EUR 695 million), for Sweden (EUR 185 million) and for Denmark (EUR 130 million, all in constant 2011 prices). Austria also benefits from a phased-out lump sum of EUR 30, 20 and 10 million for 2014, 2015 and 2016 respectively. A comprehensive view of all the corrections currently into force is available in the First Assessment Report of the Group.

nationally and commonly agreed at European level: in this respect the balance of responsibilities seems satisfying.

**8. Limit political transaction costs:** the GNI-based own resource can be strongly influenced by political, economic and financial factors internal to each Member State. When it is mostly seen as a national contribution, it can create constraints on the negotiations for the EU budget. This fosters the idea that these contributions are conditional on the vote of the national parliaments and are to compete with national expenditure, which builds political pressure on the national authorities to reduce them. The political transaction costs for the EU have increased significantly over the years as a result.

### Overall assessment

The GNI-based own resource is reliable, stable and by definition sufficient to fund the budget. There are strong mechanisms to make sure that each member state makes the due payments without delays. It is however perceived as a national contribution to the EU budget, rather than a genuine own resource<sup>28</sup>, and competing with other national expenditure.

It also benefits from the strongest support from a large majority of Member States, either because of the feeling that it remains in their control, or because it is perceived as fair. As it is currently implemented, however, together with the corrections and reductions granted to some Member States, it does result in a 'regressive' system, thereby undermining the principles of fairness, equity, simplicity and transparency. Its various adjustments in the course of budget execution can also raise stability concerns and difficulties for national budgets management.

It fulfils its main role as a revenue source, which is to provide sufficient funding for the EU budget, and guarantees that the budget is balanced. The most problematic aspect of this resource is its overwhelming dominance, which prevents progress to make the EU budget more transparent, more accountable and more visible to citizens.

*RECOMMENDATION 3 - Some elements of the current system work well, are simple, equitable, efficient and should be kept: [...]*

*- A GNI-based own resource, if used as a balancing and truly residual resource.*

### 2.2.1.2. A reformed GNI-based own resource?

As explained in point 1.2.1.2., there are improvements to be made in order to make the GNI contributions more similar in nature to an own resource, which would address the high degree of diversity in the ways Member States handle the accounting of their contribution to the EU. Only in a very few countries is this contribution classified in the general national budget as a resource attributed to the EU. In most countries, it is recorded as an expenditure of the central government.

If we want to increase transparency and simplicity of the current system, the GNI gross contributions should be recorded as revenue attributed to the EU, and in the same manner across Member States, possibly through a standardised presentation of the figures. This approach would also help national parliamentarians and any interested citizens to easily see the contribution to the EU budget.

In general, both contributions to, and monetary benefits from, the EU budget should be harmonised for the purpose of transparency, although the situation on the expenditure side is more complex and would be more difficult to address.

A further reform of the GNI-based own resource could also be implemented if there is an agreement to do so. For instance, the contributions of each Member State do not need to be proportional to GNI, and could be progressive or regressive. The financing of the European Development Fund, for instance, was based on different keys than the GNI-key for many years, although it has recently been brought closer to the GNI key.

### 2.2.1.3. The traditional own resources (TOR)

'Traditional' own resources cover the duties collected at the entrance of the single market from third countries' products. As such, they stem 'naturally' from the functioning of the customs union and the internal market, and accrue directly to the EU budget. In practice, as there is no integrated European customs' authority, it is the Member States' customs authorities that collect the amounts on behalf of the EU and forward the amounts to the Commission, after deduction of 20% retained as 'collection costs'. This percentage was 10% over the period 1970-2000, increased to 25% as from

28. One member of the group does not share the view that GNI own resources are not 'genuine' own resources and that the majority of EU expenditure should be financed by own resources other than GNI resources.

2001, and then reduced back to 20% under the new 2014 Own Resources Decision.

TOR cover customs duties levied on imports of agricultural and non-agricultural products from third countries, at rates based on the Common Customs Tariff. Duties levied on agricultural products were identified separately over the period 1970-2008, but are grouped with customs duties since then.

Sugar levies are paid by sugar producers to finance the export refunds for sugar. These levies offset expenditure of virtually the same amount.

## How do they score?

**1. Equity/Fairness:** TOR are directly linked to a central EU policy — the Single market — which benefits all Member States and citizens and whose revenues cannot be easily attributed to each Member State. This makes them resources that are 'genuinely' owned by the EU and equitable from several aspects: TOR have an equal impact on taxpayers across the EU (horizontal equity), and it can be considered fair in the sense that most TOR are normally collected from the focal points of EU trade, which also most directly benefit from this EU policy in terms of regional economic influence. However this does not mean there are not equity issues raised by some: the percentage of the collection costs that Member States retain remains a sensitive issue for the Netherlands in particular. The past increase from 10% to 25%, and the continuous high percentage applied today (20%, while the Commission had proposed to reduce it back to 10%) is considered as a 'hidden' rebate aimed at reducing the contribution of the Netherlands to EU budget financing.

**2. Efficiency:** the current system has proved efficient and has not raised major concerns in its implementation. National customs authorities make the 80% of TOR due to the EU according to commonly agreed rules and in a timely manner.

**3. Sufficiency and Stability:** the share of TOR has steadily decreased over the years, as increases in trade volumes were overcompensated by the decreases in average tariffs, following the various rounds of trade negotiations at WTO level. Since the last negotiation, however, it has stabilised around 12%. It therefore remains a non-negligible source of revenue for the EU budget.

**4. Transparency and Simplicity:** as the only fiscal resource fully transferred to the EU level, and for reasons clearly linked to an EU policy, customs duties appear as a transparent and simple resource.

**5. Democratic accountability and budgetary discipline:** TOR do not particularly score individually on this criteria.

**6. Focus on European added value:** there is a clear link between TOR and the EU customs policy.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** TOR are by definition the only tax directly stemming from the existence of the single market, and whose proceeds are logically transferred and supervised at the EU level. The transfer of fiscal power concerning them is enshrined in the Treaty.

**8. Limit political transaction costs:** the collection of TOR at national level allows pre-existing national customs authorities to continue to perform most of their tasks, and minimal central services at the EU level perform controls and oversight. Overall the implementation of the TOR rules seems satisfactory to Member States.

## Overall assessment

The traditional own resources, in particular custom duties, constitute a reliable and mostly undisputed baseline of EU revenue. They can be considered a 'benchmark' genuine own resource in as far as they arise directly from the EU being a Customs Union and from the legal competences and common trade policy linked to it.

They could serve as a model for potential future income stemming from the evolving EU Energy, Digital or Capital Markets Unions.

*RECOMMENDATION 3 - Some elements of the current system work well, are simple, equitable, efficient and should be kept: [...]*

*- Traditional own resources (customs duties), which are a benchmark of true EU revenue and whose collection process is satisfactory.*

## 2.2.2. Candidates for new own resources

In the following chapters, several possible bases for a new own resources are examined against the criteria endorsed by the High Level Group in its First Assessment Report. They are clustered into broader groups. More detailed quantitative analyses of particular own resources would require assumptions on design features and are outside the scope of this report.

CLUSTER RELATED TO THE ENERGY UNION, ENVIRONMENTAL POLICY, FIGHT AGAINST CLIMATE CHANGE (FOLLOW-UP OF PARIS COP21)

The Annual Growth Study 2015 summarised what has come to be a generally acknowledged observation in the realm of fiscal policy:

'On the revenue side, it is important to ensure an efficient and growth-friendly tax system. Employment and growth can be stimulated by shifting the tax burden away from labour towards other types of taxes which are less detrimental to growth, such as recurrent property, environment and consumption taxes, taking into account the potential distributional impact of such a shift.'

The EU budget's own resources system has usually been outside the perimeter of such considerations. However, the Group considers that a more sustainable system of own resources would play a constructive role in vertical fiscal coherence, and would establish a link with EU policies and thus also improve the transparency/accountability dimension. In this regard, the environmental and climate aspects have captured the attention of many stakeholders and tax experts. In several Member States, carbon taxes of different types and denominations are being introduced. At the EU level, a common external approach and climate diplomacy has led to the creation of the Emission Trading Scheme. In the wake of the ratification of the Paris climate agreement, and while Member States have committed to the objective of low carbon economy, it might be helpful to supplement these efforts by a coherent approach to environmental fiscal reform. Taxes can be based on production, consumption or address pollution.

The Group has examined the variants presented below, which serve to illustrate the rationale but also some pitfalls of introducing a new, environmentally motivated own resource. The Group is keenly aware of the general need to maintain a coherent overall policy approach to climate action as well as of the interdependence between the revenue-raising potential and the effectiveness in view of behavioural changes of consumers and tax payers in this area.

### 2.2.2.1. CO<sub>2</sub> levy / Carbon pricing

Carbon pricing can take different forms, either through taxation or market-based instruments. More general than a tax on fossil fuels, a carbon tax imposed on all sources of greenhouse gas emissions would have an impact on costs and prices and would aim at incentivising consumer or producer behaviour in a less

'carbon intensive' direction, an essential step to be taken in the fight against climate change.

While energy taxes already exist in all EU Member States, and are harmonised to a certain degree at EU level, carbon (or CO<sub>2</sub>) taxes are less common. As regards energy taxes, the current Energy Taxation Directive, adopted in 2003, was designed primarily to avoid competitive distortions in the energy sector within the Internal Market. It sets out common rules on what should be taxed, and when and what exemptions are allowed. Minimum rates, based mainly on the volume of energy consumed, are laid down for products used in heating, electricity and motor fuels. Above these minimum rates, Member States are free to set their own national rates.

A number of Member States have introduced specific carbon or CO<sub>2</sub> taxes but the majority of environment-related taxes, with implications for greenhouse gas emissions, are levied on energy products and motor vehicles, rather than on CO<sub>2</sub> emissions directly. Currently, Denmark, Ireland, Finland, Sweden, France and Slovenia have a carbon tax in place. However, national rates are fixed at very different levels and do not reflect the carbon price under the EU Emissions Trading System (ETS). Carbon taxes are usually designed to complement the ETS by taxing sectors not covered by the permit scheme.

The Commission's latest proposal to revise the Energy Taxation Directive (2011), planned to apply a single minimum rate for CO<sub>2</sub> emissions (20 euro per tonne of CO<sub>2</sub>) to all sectors not covered by the EU ETS. This would have 'carbon-priced' certain sectors of the economy, namely households, transport, smaller businesses and agriculture which are outside the EU ETS. After three years of negotiations, the Commission considered that the latest compromise text failed to address any of the main issues targeted by the Commission proposal. The proposal was therefore officially withdrawn on 7 March 2015.

An alternative would be an indirect carbon tax on consumption (taxing the products, not the production) according to how much CO<sub>2</sub> is emitted during the production of particular commodities, irrespective of whether all or a part of this process takes place within or outside the EU. Such a carbon tax has been analysed in some depth by a study commissioned by the Economic and Social Committee and adopts the perspective of the consumer's 'carbon footprint'. It has the advantage of encompassing the consumption of both imported and locally-produced products. CO<sub>2</sub> 'content' was measured using input-output models taking the entire production chain into account. The research concludes that, for the examined year 2011, a

tax rate of around EUR 40 per tonne of CO<sub>2</sub> emissions could have generated revenue equivalent to 1% of EU GDP. The study concedes that the results for individual Member States may differ significantly from the EU average. The effects on economic growth and a 'double dividend' would obviously depend on a commensurate compensation via reduced costs for labour<sup>29</sup>.

From the point of view of competitiveness of the EU industry, this approach presents a certain appeal, although it remains to be seen whether the most concerned economic sectors would be less prone to opposing it.

The Group's external study also recalls the model of a European carbon added tax on all goods and services, which is close in its design.

### How do they score?

**1. Equity/Fairness:** the current EU Energy Taxation Framework does not prevent that certain fossil fuels from being taxed more favourably than cleaner competitors (e.g. exemptions on fuel used by certain sectors (agriculture), tax based on fuel volume and not on CO<sub>2</sub> emissions). This creates unfair competition between fuel sources and unjustifiable tax benefits/subsidies for certain types of fuel compared to others.

The introduction of a carbon tax would allow Member States to meet their effort sharing targets, without fear of jeopardising their competitiveness within the EU and vis-à-vis third countries. It would also take into account the cross-border negative externalities (water, soil and air pollution) which by definition are not addressed by national policies alone would also avoid distortions in the internal market. Finally it would be applied to the sectors that are not currently covered by the EU ETS (an equitable tax burden would require that it is similar to the price of the emission permit).

However, from the point of view of own resources, the 'equity' of a carbon tax-based own resource might be questioned by some Member States, given that the CO<sub>2</sub> intensity of the economy differs significantly from one Member State to the other, and would be immediately benchmarked against the GNI-based own resource. However, distributional impacts can be addressed so that ability to pay is respected. A basket of own resources could help neutralise asymmetrical effects or other types of 'compensations' could be agreed. Such compensations could principally take effect on the revenue side or on the spending side of the budget.

**2. Efficiency:** the introduction of an EU-wide CO<sub>2</sub> tax would give economic actors more legal certainty and reduce compliance costs, in particular if such a tax were to replace the various environmental taxes in Member States. It would also serve the EU's and Member States' objective of reducing CO<sub>2</sub> emissions and address the problem of users not facing the full (social and environmental) costs of their actions. Depending on its design, it could significantly reduce the discrimination between EU producers in the internal and world markets. For example, a destination-based carbon tax (implemented on consumption rather than production) could avoid a loss in competitiveness of the EU vis-à-vis the rest of the world. The advantages of such tax in terms of efficiency, however, are commensurate with the technical, legal and political challenges to implement it. In any case, complementarity and/or compatibility with the ETS (scope, incentives, and economic incidence) would have to be ensured in order to avoid double taxation or contradictory objectives (as was the case in the 2011 proposal which distinguished between sectors covered by the EU ETS and those outside it).

**3. Sufficiency and Stability:** the results of the EESC study (see above) indicate that the magnitude of the potential tax base is sizeable enough cover a large part of the EU budget.

As with any 'polluter pays' scheme, there is an inherent balance between revenue generated and (desired) behavioural changes. A carbon tax should primarily aim at changing energy consumption behaviour, within the larger perspective of moving to a low-carbon economy. The provision of a stable source of revenue would therefore only be a secondary objective.

In theory, the stability of such a tax could be improved by providing for a flexible rate. It could even be designed as a residual own resource based on the carbon emission of each Member State compared to the overall EU emissions (replacing the GNI-based own resource), although the political feasibility of such proposal in the current context would appear low. Measuring tools of CO<sub>2</sub> emissions are already in place in Member States, and can be used to calculate a theoretical CO<sub>2</sub> emission base for each Member State (similar to the existing VAT base calculation).

**4. Transparency and Simplicity:** the introduction of a CO<sub>2</sub> tax at European level would bring more transparency and simplicity to carbon taxation, thanks to tax harmonisation and the avoidance of double taxation. Concerning the EU budget, transparency and simplicity would depend on the implementation and

29. It is also stated that beyond the examined 'first round effects', 'the economic changes induced by a reaction of consumers to the changes in relative prices are not covered and require the development of more complex models, dealing with the economic effect of introducing a CO<sub>2</sub> emission tax'.

making available rules for a carbon tax as an own resource.

**5. Democratic accountability and budgetary discipline:** an own resource based on carbon taxation would reduce GNI-based contributions and therefore respect the budgetary discipline enshrined in the own resources system. It could significantly improve democratic accountability if the link with the objective of environment protection is clearly made both at EU and Member State levels.

**6. Focus on European added value:** the EU and its Member States play a leading role in the international efforts to protect the environment and the climate. A common, coherent carbon pricing policy including a CO<sub>2</sub>-taxation element at EU level would be more effective overall than a fragmented landscape of differing national approaches, in terms of environmental integrity, economic efficiency as well as political impact. Studies have shown that a carbon / CO<sub>2</sub> tax could also contribute to economic growth due to the significant revenues that can be raised while having a smaller negative macroeconomic impact than other tax options, in particular if implemented through a 'tax shift' from existing taxes which are more detrimental at macro-economic level.<sup>30</sup>

**7. Subsidiarity principle and fiscal sovereignty of Member States:** as long as the carbon tax is introduced by a directive, Member States will still have to implement the directive by introducing national legislation (or adjusting existing legislation), since the actual levying of the tax would take place at Member State level. The directive would include minimum levels/rates of taxation. The Own Resources Decision (including ratification requirement) would provide for the revenue-sharing arrangement and the principle of transfer of such tax to the EU budget. The diminished level of national discretion in the field on environmental fiscal reform would have to be benchmarked against the effectiveness and efficiency of a patchwork of individual, non-coordinated measures.

**8. Limit political transaction costs:** the introduction of a Carbon/CO<sub>2</sub> tax is very likely to encounter strong hostility from the transport and fuel industries, which currently benefit from preferential tax regimes. Such tax should also be envisaged as part of a more comprehensive package in order to accommodate Member States more dependent on carbon-based fuels so that the fairness of the system is ensured. A tax on consumption resulting in price increases for certain products would likely encounter scepticism, if

not hostility, too and it would have to be accompanied by a proactive communication about the purpose of the tax and the compensatory measures (e.g. in the field of taxation on labour costs and/or lower GNI-based contributions).

#### Overall assessment

A European approach to CO<sub>2</sub> taxation would not only reinforce the EU's credibility as a world leader in environmental protection and the fight against climate change, it would also be more efficient and create a level playing field for economic actors across the EU. CO<sub>2</sub> taxation would not be applied to renewables, providing them with an advantage compared to the conventional fuels they are competing with. A carbon tax-based own resource would thus have a clear link between a fundamental EU policy objective and the financing of its own budget.

If such an own resource is introduced and successful in diminishing the production or consumption of carbon and CO<sub>2</sub> emissions, the revenue stemming from it should logically decrease in time, which is a weakness from the strict point of view of the sufficiency of this resource. However, the financing of the EU budget should only be seen as a secondary objective, while its primary objective is decreasing carbon consumption, in line with the commitments undertaken internationally and at the EU level, notably the target to reduce carbon emissions by 40% in 2030 compared to 1990, to be followed by further efforts to reach cuts equivalent to 80-95% by 2050.

#### 2.2.2.2. Inclusion of the EU Emission Trading System proceeds

The EU Emissions Trading System (ETS) has been introduced in several phases as the main instrument to combat climate change and reduce industrial greenhouse gas emissions. It currently covers around 45% of total greenhouse gas emissions from the 28 EU countries. Emission allowances are attributed to each Member State, and are then auctioned. A market stability reserve was created recently to address the substantial surplus of certificates on the market resulting from the economic crisis, which had reduced emissions more than anticipated.

The EU ETS was created with the primary purpose of lowering emissions to a pre-defined level. It was not created with a view to deliver a steady, stable flow

30. Vivid Economics, Carbon taxation and fiscal consolidation: the potential of carbon pricing to reduce Europe's fiscal deficits, report prepared for the European Climate Foundation and Green Budget Europe, May 2012.

of proceeds or to transfer part or all of its revenue to the EU budget as an own resource. This option was examined for the first time in the 2010 budget review, but the subsequent Commission proposals of 2011 did not take it further, essentially for two reasons:

- » the economic impact of the ETS varies significantly from one Member State to the other due to the fact that the national economic structures and energy mixes are different;
- » 50% of auction revenues are already earmarked to be used for climate-related actions.

In the larger perspective adopted by the present Report, however, the destination of the ETS proceeds should be re-examined.

## How does it score?

**1. Equity/Fairness:** Phase 3 of the ETS (2013-2020) has brought significant harmonisation of the system at European level: a single EU-wide cap on emissions instead of previous national caps, the progressive increasing share of auctioning — rather than free allocations — to allocate allowances (40% in 2013), harmonised allocation rules for the remaining free allocations, the inclusion of more sectors and gases and the creation of a 300 million reserve to fund innovative renewable technologies and carbon capture and storage. While these changes contribute to greater harmonisation in the treatment of individual installations, they do not directly change the underlying differences between the energy sector and the economic structure of Member States.

**2. Efficiency:** the ETS as it currently exists applies to all EU-28 Member States, which therefore creates a common basis on which an EU own resource could be created (no differentiation between Member States). Similar schemes have even been developed in other parts of the world. The participation of EEA-EFTA countries and the expanded scope encompassing the aviation sector will also have to be carefully considered.

**3. Sufficiency and Stability:** data in this area are scarce. The total revenue generated by the auctioning of ETS allowances in the year 2013 in all EU-28 was EUR 3.6 billion (around 2.5% of the total EU budget). Under a strengthened legal framework, the proceeds might rise again, but the effectiveness of the ETS will also hinge on the international post-Kyoto climate regime and the fact that the decline of ETS revenue is built in the system, with the reduction target in emissions from sectors covered by the EU ETS being 21% lower in 2020 than in 2005 (and 43% lower by 2030). This would raise sufficiency issues if it were proposed as an Own Resource. The demand has been consistently

low so price levels and auctioning proceeds have in any case been significantly below the tentative estimations of the 2010/11 budget review (up to around EUR 20 billion by 2020). Stability of revenue is not the primary aim of any cap and trade scheme. Potentially low or volatile income must therefore be factored in.

**4. Transparency and Simplicity:** collection and administration of current ETS revenue is ensured at the national level, by authorities designated by Member States. Collecting it as an own resource would simply entail a simple transfer of part or all of this revenue to the EU level.

**5. Democratic accountability and budgetary discipline:** an own resource based on ETS would reduce GNI-based contributions and therefore be in line with the budgetary discipline enshrined in the own resources system. As for other carbon taxes, it could improve democratic accountability if the link with the objective of environment protection is clearly made both at EU and Member State levels.

**6. Focus on European added value:** as with other candidates based on carbon or other environmental taxes, an own resource based on the ETS would have a strong relation to European added value due to its direct link to the single market and to the objectives of EU environmental policy. A common, coherent approach is already a reality, but the link with the EU budget would make even more sense as this source of revenue has been created at EU level.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** the ETS strongly focuses on cross-border activities and their impact in terms of emissions. It has increasingly harmonised rules (phase 3) which contribute to creating a level playing field within the single market and is established at the appropriate governance level from the point of view of subsidiarity. Attribution of its proceeds as an own resource would be decided by Member States.

**8. Limit political transaction costs:** political transaction costs would be limited as the essential tools for enforcing the collection of such revenue are already in place. However, this is currently revenue for national budgets and even if GNI contributions decreased as a result of ETS proceeds being attributed to the EU budget, such change would certainly encounter strong resistance.

## Overall Assessment

An ETS-based own resource, as any other resource stemming from the environment/climate change/energy policy areas, would have the advantage of establishing a clear link between the financing of the

EU budget and one of the essential policy objectives of the EU. Its specific focus on cross-border activities and their related impact on the environment further reinforces the link with European added value and a better functioning single market.

In terms of public visibility and accountability, there is a strong justification to attribute the proceeds of an EU wide trading scheme, based on EU-wide emission reduction targets, to the level at the origin of this policy.

The essential weaknesses of the ETS-based own resource are the relatively small amounts concerned, its lack of stability from one year to the next and the perception that it is less fair than the GNI-based own resource since it was attributed as national revenue. For all these reasons, rather than a 'fully-fledged' own resource, the Group would consider it as a better candidate for 'other revenue' to the EU budget. Such a change could also be implemented more easily via a reform of the ETS directives.

### 2.2.2.3. Motor fuel levy (taxes on fossil fuels/excise duties)

Motor fuel taxation<sup>32</sup> is currently a significant source of national income in all EU Member States and it is the most relevant source of tax revenue in the transport sector. Taxation level is decided by national governments, within the limits (reduced rates of taxation and exemptions) established in the Energy Taxation Directive.<sup>33</sup> The accruing proceeds constitute national budget revenue or in some cases sub-national entities' revenue.

From the point of view of own resources, two scenarios could be envisaged:

- » a full transfer of the revenue collected by from Member States from the motor fuel tax to the EU level;
- » a partial share or percentage of the motor fuel tax collected by Member States.

The first scenario would represent a major systemic and very visible shift from the present system, both at national and EU levels. This shift would most probably encourage harmonisation and at least neutralise the tax competition effects at national level. 'Centralisation' of such tax at the European level could be justified legally within the current Treaty under Article 192 or

Article 194 TFEU, which respectively lay down a legal basis for fiscal measures in relation to environmental purposes and energy policy purposes. These provisions, which were introduced by the Lisbon Treaty, have not been used until now.

Such an own resource could not only finance a sizeable share of the EU budget, it would also provide for a European public good (environment protection) and be coherent with the European Energy Union initiative as regards the decarbonisation of the transport sector.

The second scenario implies that a partial share or percentage of the already existing taxes on motor fuel would be attributed to the EU as a new own resource. It would probably be more acceptable for Member States, although it would not serve the purposes of harmonisation, neutralisation of fiscal externalities or shifting to a common and stable EU environment-related fiscal policy so well as in the first scenario.

#### How does it score?

**1. Equity/Fairness:** a motor fuel tax would respect the principle of 'user-payer' or 'polluter pays', if applied to consumers as well as to sectors and industries which currently benefit from significant exemptions. Under the hypothesis of a complete transfer of such tax to the EU, this could trigger fiscal harmonisation, address negative externalities and inequality of fiscal treatment between road transport users in Member States. It would also provide for a common fiscal position towards external competition. However, as existing national taxes constitute a significant share of national budgets and have different weights throughout Member States, it can be expected that finding the right and equitable balance will require some forms of compensation or progressiveness.

**2. Efficiency:** economically, in as far as some 'market failure' would be addressed (distortions due to 'tank tourism'), a common taxation scheme would improve overall efficiency and reduce distortions within the single market. In terms of collection, a motor fuel tax would be very efficient since it would rely on existing mechanisms. Such taxes are already collected by national authorities.

**3. Sufficiency and Stability:** a motor fuel tax has a very significant revenue potential and constitutes one of a limited number of bases which could actually cover all or a very large share of EU budget needs, depending on its design (full or partial transfer). In

32. This term covers fuel used in transport but also in stationary motors in manufacturing and other activities: agriculture e.g.

33. Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity (OJ L 283, 31.10.2003, p.51).

addition, the consumption levels of motor fuel seem to be rather stable. If the tax is strongly geared towards environmental protection, there could be a long-term built-in decrease in revenue as consumers would tend to change their behaviour.

**4. Transparency and Simplicity:** a motor fuel tax would probably be one of the most simple and transparent own resource for the taxpayer, in particular if the percentage/amount attributed to the EU budget is shown on the receipt and if the base for this tax is fully harmonised and the collection centralised. However, it would only show the 'costs' of the EU, while the benefits would remain hidden.

**5. Democratic accountability and budgetary discipline:** in the case of a complete shift from the motor fuel tax at national level to the EU level, the national parliaments would lose their scrutiny of a national tax and Member States in general would lose their margin of manoeuvre to adjust this tax according to the economic conditions. Democratic accountability and budgetary discipline would need to be ensured at European level through an enhanced role and responsibility of the European Parliament (in particular on the taxation directives which would accompany the Own Resources Decision). As far as budgetary discipline is concerned, a motor fuel own resource would decrease the GNI-based own resource and therefore ensure budgetary discipline.

**6. Focus on European added value:** like other candidates based on a carbon or environmental tax, a motor fuel own resource would reinforce the credibility and efficiency of the action of both the EU and its Member States as leaders in the international efforts to carry forward the fight against climate change. A common and harmonised motor fuel tax would have more impact than national taxes in terms of environmental integrity, economic efficiency as well as sending a political signal to the international community.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** the collection of such tax would still be ensured by Member States' collection authorities, similar to the traditional own resources (custom duties and sugar levies) collection.

**8. Limit political transaction costs:** the introduction of an EU motor fuel tax could encounter significant opposition from Member States who use such tax as an important and flexible fiscal tool, or by regions or industries that benefit from reduced rates or even exemptions.

## Overall assessment

In both scenarios of a full or partial transfer of this tax to the EU level, a motor fuel tax has strong potential for an own resource given the significant volume of taxation it represents in all Member States and its relatively harmonised base that would facilitate its implementation and the stability of its revenues.

In addition, it would contribute in parallel to environmental protection and thus to a genuine European common good, the EU being better placed than each of the 28 Member States to address negative externalities and build a common climate policy. The link with environmental goals would be particularly strong if the tax was differentiated on the basis of the CO2 content of fuels. Furthermore, it would also contribute to the goal of internalising transport externalities in the context of the decarbonisation objective of the transport sector. As a further step, it could lead to the creation of a single market in motor fuels, correct the existing deficiencies such as 'tank tourism' or the big differences in prices at the pump (without taxes).

The major obstacle to a motor fuel tax becoming an own resource is its political acceptability. Opposition would probably be mutually reinforced by administrations reluctant to lose such a powerful fiscal tool, and by sectors or regions which benefit from a better fiscal position than competitors in this regard. The lack of agreement over the new Energy Taxation Directive proposed in 2011 is a reminder that these taxes are very sensitive.

From the point of view of own resources, the erosion of the tax base is to be expected in the long term if consumers change their consumption significantly, and if the EU commitment to implement the decarbonisation of the transport sector is swiftly endorsed. The tax base would then shrink progressively due to the decarbonisation of transport. If desired, this type of digressive revenue evolution could be controlled for in the tax' design (the tax could evolve or not only be levied on current motor fuels but also, progressively, on CNG, LNG, hydrogen and electricity ).

## 2.2.2.4. Electricity tax-based own resource

Taxation on electricity already exists in all EU Member States. Taxation level is mostly decided by national governments and the accruing proceeds constitute national public revenue. EU legislation sets minimum levels of taxation and obligatory exemptions.

There are different types of taxes on electricity that can be implemented:

- » taxes on electricity production (eg. Environmental/pollution taxes);
- » taxes on the transport of electricity (eg. tax or levy on the use of public space);
- » taxes on the sales of electricity (eg. consumption taxes, environmental taxes).

The first two types of taxes are collected from electricity companies. The third is paid by electricity consumers (households and companies).

Consumers spend on average 6.4% of their total consumption on energy. In the context of the Energy Union initiative, the Commission has presented important proposals for redesigning the EU electricity market. It is expected to result in better interconnections security of supply, more integrated and transparent markets, more choice for energy consumers and efficiency gains. A fundamental transformation of the electricity market should deliver tangible benefits for households and companies. The upcoming 'Heating and Cooling strategy' is intended to reduce related electricity costs.

A common electricity tax or levy at European level would, in principle, be justified on the grounds that internal market integration will lead to economies of scale, benefiting the production sector, and ultimately, consumers. In addition, current efforts at creating interconnected electricity grids might justify a more coherent taxation at European level. From the strict point of view of EU budget financing, the potential volume of such tax makes it an appealing candidate to finance a large share of revenue. The EU could also link this potential own resource to EU environmental and energy-saving policies. However, any reform proposal should take into account that the production of electricity is mostly covered by the Emission Trading System ETS. The 'architecture' of the economic incentive structures should remain coherent.

Most analyses seem to favour taxation on electricity consumption rather than production and transport, mainly for fairness and simplicity reasons:

- » It is easier, less costly and more transparent to collect from consumers through the electricity bill. All consumers already have mandatory electricity bills, with taxes already included on it. An EU electricity tax could therefore appear clearly indicated in the bill for transparency purposes and EU contribution awareness.

Additionally, the control of the usage and payment is already being done by the electricity companies, making this tax less prone to tax evasion.

- » There seems to be proportionality between electricity consumption and income level. Richer regions tend to consume more electricity than poorer ones. Taxing consumers might therefore have a redistribution effect. At the level of private consumers, however, proportionality seems to be lower since poor households would suffer a bigger impact in electricity prices than richer households. Such effects could incite demands for balancing or compensation mechanisms, both at European and national level (subsidies and/or exemptions), which in turn would lessen the simplicity and transparency of the tax.

#### How do they score?

**1. Equity/Fairness:** an electricity tax on consumption would respect equity and fairness at macroeconomic level since the consumption trends seem to show that the level of electricity consumption is related to the level of income. The distributional impact of such tax at national or even regional level would have a clear equity and 'ability to pay' dimension. Harmonisation efforts would be very high for countries where such taxation is very low.

**2. Efficiency:** economic efficiency, in a larger, more integrated market would increase with the harmonisation of levies and taxes on electricity. The collection of an electricity tax could be organised very efficiently compared to other potential own resources. Current taxes on electricity are already efficiently collected by national authorities, via distribution companies. Moreover, because electricity is a basic consumption good and cannot be 'replaced' easily by another, such tax would not entail a similar trade-off between revenue generated and evolution of consumers' behaviour than other polluter pays' schemes.<sup>39</sup>

**3. Sufficiency and Stability:** the introduction of an electricity tax as an own resource could provide for a very large share of revenue depending on the share or percentage applied. K. A. Konrad (see footnote 41), based on Eurostat figures, calculates that given an overall annual production of roughly 3.1 million GWh, a unit tax of 1 cent per kWh could generate about EUR 31 billion in tax revenue. The consumption levels of electricity seem to fluctuate according to the income levels of consumers, therefore having a similar, rather low, volatility to the GNI.

39. On the flipside, it would thus be inconsequential to label such a revenue sources as an 'environmental tax'.

**4. Transparency and Simplicity:** the collection of an electricity tax is simple, in particular if applied as a share or percentage of the total tax on the electricity bill. National authorities already collect tax on electricity and for transparency purposes the EU share could be made clearly visible as well on the consumers' bill. Complexity would depend on how the electricity tax is used as a policy tool (e.g. as social policy) and the related tax reductions and exemptions. The design of the tax would therefore need to take these differences into account and provide exemptions.

**5. Democratic accountability and budgetary discipline:** no particular role on enhanced accountability or budgetary discipline.

**6. Focus on European added value:** European citizens, as consumers and actors of the EU internal market, will be able to feel a clear link between the benefiting of such space and the financing of the EU policies. It could also play a role in relation to the EU environmental and energy-saving policies. However, in order to meet the Energy Union objective of electricity price reductions for EU citizens, an electricity tax would have to be implemented not as an additional burden in electricity taxes but as a shift from national tax revenues to EU revenue.

**7. Subsidiarity principle and fiscal sovereignty of member states:** as the collection of such tax already exists in Member States, the European tax could also be collected at the national level, similar to the traditional own resources (custom duties and sugar levies). A new Own Resources Decision, after adoption and ratification by all Member States, would provide the revenue arrangements and the principle of transfer of such tax to the EU budget. In so far as some surcharges are levied by municipal or regional levels — some of them even earmarked for specific uses — a differentiation of the distribution of proceeds between different levels of governance is already common practice.

**8. Limit political transactions costs:** political costs would be high for a number of Member States because current EU legislation sets very low minimum levels of taxation and there are big differences between the tax rates of different Member States. A minor tax increase for some (Denmark, Germany) could be quite considerable for others (Bulgaria). Furthermore, despite the re-distributive nature of the tax as identified in K. A. Konrad's paper, an electricity tax could also encounter hostility from high electricity consuming Member States and industries. Arrangements at national and/or EU level would most probably be required to make such a tax acceptable.

## Overall assessment of the Electricity tax-based own resource

Depending on the design of the tax and the optional and obligatory tax exemptions or reductions, an electricity tax-based own resource charged on all consumers could be simple, fair and transparent. It could also be a stable source of revenue for the EU budget. Taxation at EU level could also promote the harmonisation of electricity taxes in Member States, furthering potential gains of the internal market.

Such an own resource would also create a link, albeit rather weak, between some EU policy objectives on environment and energy savings and the financing of the EU budget, without entailing a built-in risk for the stability of the own resource's proceeds as in other 'polluter pays' schemes'.

Weaknesses of such a proposal would mostly concern political transaction costs, probably from industries and regions with high electricity consumption (although it is demonstrated that these tend to be richer regions, and thus the proposal would be equitable from a macroeconomic perspective) and from poorer households. The demarcation of an EU-level electricity tax from the scope of the ETS (targeting the production of electricity) would have to be carefully explained. The visibility of the EU share of the electricity tax should also be appraised in all its dimensions: transparency to taxpayers would be ensured, but, again, such a presentation would risk highlighting the costs of the EU and not its benefits.

### CLUSTER RELATED TO THE SINGLE MARKET AND COMMON TAX POLICIES

#### 2.2.2.5. CCCTB, EU corporate income tax

An EU corporate income tax is not a new idea and has been supported since the early 1990s, both in academic circles and in previous reviews and analyses by the Commission and the European Parliament. Like any other so-called EU tax (see point 1.2.), what is meant here is an own resource based upon minimal harmonisation of national corporate tax systems, in accordance with national fiscal competences.

Member States have always been extremely reticent to even discuss matters of direct fiscality. It is only in recent years that the prospect for such an endeavour has become less remote, in the context of the disclosures and leaks about tax practices from many multinational

firms and wealthy individuals, and about the damaging effects of the increased race to the bottom between national fiscal authorities to obtain or only maintain their competitive advantage.

The European Commission has recently put forward a comprehensive legislative package aimed at 'building a fair, competitive and stable corporate tax system', and in particular to re-launch the common consolidated corporate tax base (CCCTB). This initiative exclusively concerns the coordination of such tax and not the possible use of its revenue for the EU budget. However, a new own resource could be envisaged in the future. It would imply that a common share of this CCCTB would be transferred to the EU level.

#### How does an EU CIT score?

**1. Equity/Fairness:** CCCTB is instrumental in making the single market more competitive and fairer, by ensuring that every company, no matter its size, pays its taxes where it makes its profits. It is therefore strongly linked to the fight against tax avoidance which has become a top priority in the EU and internationally.

**2. Efficiency:** one of the main objectives of CCCTB is to create a simpler and more business-friendly tax environment in the EU. As one of the first benefits, Member States will need to apply the same rules for calculating companies' taxable profits, which will simply eliminate the loopholes between national tax systems, and eliminate transfer pricing in particular, which accounts for around 70% of all profit shifting in the EU.

**3. Sufficiency and Stability:** depending on the rate applicable to the CCCTB once this is established and consolidated, an EU corporate tax income could represent a substantial share of EU financing. Revenues from corporate taxes represent 2.4% of EU-28 GDP (2014 Eurostat figures), with substantial differences in Member States, ranging from 1.4% GDP in Hungary, Lithuania and Slovenia to 4.4% in Luxembourg or 6.4% in Cyprus.

**4. Transparency and Simplicity:** transparency is the foundation of the CCCTB, because it is only when Member States agree on automatic exchange of information on taxation of multinational companies, and on the now infamous tax rulings practices, that coordination will be possible to ensure that tax is paid where profits are made, and to deal with countries that refuse to play fair in tax matters. It would allow businesses to enjoy a level playing field, legal certainty and minimal obstacles when operating across borders. It would also, at the stage of the consolidated base, allow them to fill out only one set of tax papers for their entire EU operations, which would benefit large and multinational companies,

but also smaller and growing companies for which 28 different tax systems is a hurdle.

**5. Democratic accountability and budgetary discipline:** by eliminating hidden preferential regimes and harmful tax rulings due to the increased transparency, the CCCTB is one of the most efficient tools to restore confidence in national tax systems and enable Member States to refocus their resources on growth-friendly taxation and to support wider socio-economic needs. It appears as an appropriate and much-needed response to the rise of dissatisfaction which feeds populism all over Europe.

**6. Focus on European added value:** the European added value in fiscal matters is at its highest in the case of the CCCTB, given its close link to deepening the single market and making it fairer.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** as for the VAT base when its harmonisation was agreed upon in 1970, the harmonisation necessary before creating an own resource based on corporate tax will require changes in national fiscal policies. On the basis of empirical data and in particular the fierce tax competition on corporate taxes which is led by a few 'small countries located in the centre of the EU', a harmonised tax base at EU level appears to be a means to regain fiscal sovereignty, notably for those Member States which do not have any alternative other than entering the race to the bottom for fear of a competitive disadvantage. For this reason as well, it is fully in line with the subsidiarity principle as only at the EU level can such negative externalities be tackled.

**8. Limit political transaction costs:** given the very diverse fiscal landscape for corporate taxes and the positioning of a small number of countries at the head of tax competition in this area, political agreement will be difficult, although the numerous recent tax scandals have increased the pressure to act in many Member States. The capacity to convince that such common corporate tax base will bring economic dividends also for these small countries will be essential to find consensus.

#### Overall assessment

A new own resource based on a common consolidated corporate tax base would score well on many crucial criteria identified for own resources, in particular equity, efficiency, democratic accountability and European added value, on the condition that the tax base is actually consolidated and sufficiently large to yield sufficient revenue. As it is currently envisaged, the CCCTB is limited for the purpose of own resources because it is

built on the voluntary registering of companies, except for those with annual consolidated group revenue of more than EUR 750 million, for which registering will be mandatory. It remains to be seen if this high mandatory threshold would suffice to produce significant revenues or if this aspect would need to be revisited if the CCCTB is envisaged as a future source of revenue for the EU budget.

## 2.2.2.6. Financial Transaction Tax

The idea of a financial transaction tax is not new and was proposed in 1936 by the economist John Maynard Keynes 'as a way to discourage the kind of speculation that fuelled the stock market bubble that led to the Great Depression.'<sup>40</sup> Similar taxes were advocated more recently by economists Joseph Stiglitz, Larry Summers and James Tobin, the latter proposing to tax short-term currency exchange transactions in order to reduce speculation in international currency markets. Financial transaction taxes are in general not limited to currency markets and also target transactions in shares, bonds and derivatives.

Other economists, notably the IMF, have rejected the proposal of a financial transaction tax and have suggested other instruments to tax the financial sector.<sup>41</sup> Other examples are described under point 2.2.2.7. below, although they would be more adequately designed in the context of the euro area than in the context of the EU budget (see point 3.2. as well).

The Commission proposed that a financial transaction tax be introduced at EU level in 2011, in the aftermath of the 2008 financial crisis and with the purpose of ensuring that the financial sector — which is largely exempted from taxation — makes a fair and substantial contribution to public budgets. It also proposed that a share of this tax be used as an own resource for the EU budget. In the Commission design at the time, the possible revenues from the FTT were estimated at above EUR 50 billion per year, two thirds of which would have accrued to the EU budget and would have reduced Member States' contributions based on GNI accordingly. By 2020, assuming that the taxable transaction volume would develop in proportion to the development of nominal GNI, about EUR 54 billion could have been raised to finance the EU budget. This would have reduced the GNI-based contributions by around 50%. The EU-wide FTT was also seen as a first step

towards promoting it at global level, which is ultimately the most efficient level for the implementation of such tax. Member States could not reach consensus on the creation of the FTT, and a group of 11 Member States subsequently engaged in 'enhanced cooperation' to create a common FTT harmonised among them. Discussions on this proposal are still ongoing in the Council. In parallel, the proposal to use some of its proceeds as an own resource to the EU budget has been abandoned.

### How does FTT score?

**1. Equity/Fairness:** the implementation of a financial transaction tax would have positive equity effects between economic actors, as it would at least partially compensate for the tax advantage of the financial sector, which is exempted from VAT on most financial services and benefited from state aid in times of crisis. From the perspective of horizontal equity however (between Member States), it is perceived by some as unfair, since a high volume of financial transactions and a large number of financial institutions are concentrated in a limited number of Member States. This is one of the reasons why discussions on the distribution of the proceeds under the current proposal have encountered so many difficulties. On this particular point, attributing the proceeds to the EU level would provide a sound and justified solution due to the close links between the existence of the single market and the development of the highly mobile financial industry in Europe.

**2. Efficiency:** the introduction of a common system for the FTT would reduce the current possibilities of tax avoidance within the FTT jurisdiction (the jurisdiction of Member States participating in the enhanced cooperation), ensure a more coherent tax framework and eliminate a source of fragmentation of the current internal market, at least within the FTT jurisdiction. The action at EU level could prove both more effective and efficient than uncoordinated action by Member States given the level of cross-border activity and high mobility of the tax bases.

**3. Sufficiency and Stability:** the high volatility of financial transactions could generate unpredictability of income, which remains true at any level of taxation in this case. As concerns the volume of expected revenue from FTT, it would depend on the final design of the tax itself, notably the tax rates, the tax base and assumptions on the market reactions. For the 11 Member States participating in enhanced cooperation,

40. Financial transaction taxes: an overview, Leonard E. Burman, William G. Gale, Sarah Gault, Bryan Kim, Jim Nunns and Steve Rosenthal, Tax Policy Center, Urban Institute and Brookings Institution, January 2016.

41. The IMF (2010) has suggested to combine a key for bank resolution with a financial activities tax, see IMF (2010): A fair and substantial contribution by the financial sector. Final Report for the G-20 and Background Material, IMF, June 2010.

preliminary Commission estimates in 2013 found that the revenues of the tax could be between EUR 30 and 35 billion on a yearly basis, if the original FTT proposal had been applied to the EU-11. These estimates would probably have to be adjusted downwards in case of:

- » a narrower tax base due to a different scope compared to the 2013 Commission proposal (e.g. exempting certain types of financial instruments or transactions or actors);
- » the application of different taxable amounts or lower tax rates, for derivatives for example
- » a gradual phasing-in, resulting in time lags;
- » different criteria or a different order of criteria to be applied to the territorial application of the tax (e.g. changing of the order of application of residence and issuance principle or changing of other principles.)

It is not possible to precisely quantify these elements at this stage. The revenue estimates for all participating Member States would have to be reassessed once all these elements can be quantified.

**4. Transparency and Simplicity:** the FTT aims at using a single harmonised tax in the FTT jurisdiction for the financial sector, which will provide a simpler tax framework for the companies covered by it than different national ones.

**5. Democratic accountability and budgetary discipline:** insofar as the FTT proceeds would accrue to the EU budget, the GNI-based national contributions to the EU budget would be lowered, thereby having no impact on the volume of the EU budget and potentially giving extra room for manoeuvre for national budgets, notably for the Member States where no such tax previously existed (7 out of 11). In addition, the Commission has initially made provision for the minimum tax rates to be set in an implementing regulation decided with the consent of the European Parliament.

**6. Focus on European added value:** the FTT is a textbook example of a tax whose implementation can be better achieved at EU level (or global level) due to the high mobility of its base. While an EU-wide FTT could not be achieved at this stage, enhanced cooperation in this matter would already improve the functioning of the single market once the common FTT is implemented on their territory, compared to fragmented, differing national approaches, although to a lesser extent.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** as with other tax-based own

resources based on Article 113 TFEU, the FTT is not as such a 'European Tax' but aims at harmonising what is necessary to ensure the functioning of the single market and avoid distortion of competition. It is based on a Council directive and must be transposed by Member States in their national legislation. Own resources arising from such a tax would rather constitute a revenue-sharing arrangement than a new EU tax, and require a change of the Own Resources Decision at unanimity in the Council and after ratification by national parliaments.

**8. Limit political transaction costs:** given its multiple objectives in relation to financial discipline in particular, and the popularity of such a tax in most Member States, the political transaction costs of the FTT were consistently considered low. In addition, the tax is to be levied and collected by Member States and would therefore not entail significant administrative costs or changes. For the 7 out of 11 Member States which do not already have a non-harmonised national FTT in place, it would constitute a new revenue stream and give national governments extra room for manoeuvre.

#### Overall assessment

The first objective of the FTT is economic and geared towards the proper functioning of the single market and avoiding distortion of competition. The designation of its proceeds as an own resource comes as a second objective, although it is a good example of a tax which is probably difficult — if not impossible — to implement in a single Member State for fear of fiscal competition, notably in smaller Member States, and because the tax base is extremely mobile. Ideally such tax should be implemented worldwide.

The FTT under enhanced cooperation could probably still be a viable basis for an own resources if its neutrality towards non-participating Member States can be established. However, this would introduce a kind of differentiation, and thus a layer of complexity in the revenue system. For this reason, it could be a good candidate to fully test the proposed versatility of a new system and, instead of making it an own resource, enter its proceeds into the budget via the 'other revenue' approach, and even perhaps earmark it for a specific purpose which would link it to an EU policy and make it more visible.

### 2.2.2.7. An alternative option to FTT: a bank levy or financial activities' tax

In the aftermath of the great financial crisis of 2008, several initiatives were envisaged to ensure that the financial sector contribute to the costs of the crisis borne by public budgets and be made more resilient to face future shocks. Financial transaction taxes were particularly popular options, but alternatives have also been analysed, notably in the IMF's report of 2010 to the G-20.

At the EU level, unanimity could not be found on a specific instrument, but the Banking Union was created for the members of the euro area, in particular to increase the resilience of banks against future risks of default or systemic crisis, and led to the creation of two instruments: the Single Supervisory Mechanism and the Single Resolution Fund. A European Deposit Insurance Scheme (EDIS) will complement these. The new arrangements relating to the resilience of the banking sector are for the moment financed by fees levied on the banks and tailored on the assessment of the bank specific risks.

In the future, the banking sector could also raise other resources, for instance if it were submitted to the CCCTB in the future, or through a financial activities' tax (FAT) which would target the base of the 'value added' of financial services which has so far been exempted from the VAT. An FAT, for example as proposed by the IMF, would tax the gross margin, i.e. all remunerations, not just profits of banks: in substance the tax base is value added. The proceeds from such sources of revenue could be earmarked for the banking sector itself, could be used in the context of a future euro area budget, or even become own resources for the EU budget if Member States agree to it. Fiscal sovereignty of Member States would not be jeopardized. Member States would retain full jurisdiction on the tax rate, and would only devolve part of the revenues to the euro area or EU level in a revenue sharing arrangement. In this respect, it would be a similar proposal than the current VAT-based own resource.

Depending on its design, and in particular whether it would concern the banks and financial institutions of all or only some Member States, such a tax-based resource could fulfil important criteria such as fairness, transparency (of origin and use), as well as 'link to policy'. It would score well on most criteria, notably equity, transparency and simplicity. The origin and purpose of such own resource would be clear, whether it would involve banks being taxed in order to finance Funds which will compensate individuals and firms in

case of a bank default, or prevent a systemic financial crisis.

Even if such tax were to finance a euro area project only, it would bring added value by improving the functioning of the banking union and its institutional setting. It would also fulfil the principle of subsidiarity in the sense that it would be created at the adequate level of action in a single currency union.

One of its main benefits would be the gain in efficiency in the functioning of the Banking Union: it would create a level playing field in the area of taxation (whether it is based on CCCTB or on a Financial Activities' Tax), an important source of inequalities and distortions, in particular through the harmonisation of accounting rules. Indeed, although the banking sector is largely familiar with IAS/ IFRS rules, accounting for financial reporting at individual bank level is still largely based on national GAAPs. IAS/IFRS are mandatory only for consolidated financial reporting of listed banks. This would also have a positive impact in respect of supervisory regulation: capital requirements are calculated on the basis of financial reporting, hence depend on accounting rules.

However, as regards the political transaction costs, i.e. for the possibility of reaching a consensus on such proposal, the prospects are very limited in the short run. As explained above, a different agreement is currently being implemented for the SRF and the EDIS (a public scheme of compulsory risk-tailored fees levied on the banks). In addition, the CCCTB as currently proposed excludes the financial sector. An additional scheme concerning banks therefore appears very unlikely at the moment and would probably not even be desirable. But in the medium-term perspective of a reform of the whole system of own resources, it may make sense to move from the financing of a Fund with risk specific fees to a financing based on corporate income tax or on added value. From the point of view of political economy, although both systems place the cost of financing the SRF and the EDIS on the banks, the system based on specific risk-tailored fees inevitably contains a degree of approximation and of technical and "political" compromise and may be perceived as more technical and abstract and less appealing to the large public opinion than taxing the profits of the banks.

The approach of using proceeds from a certain sector (e.g. financial) to fund the needs of a particular policy area (here: the Banking Union) would, a priori, run counter to the universality principle. It may be an interesting case study to explore whether more targeted use of earmarking of revenue may nevertheless be an acceptable way forward under certain conditions (see also point 3.2.).

### 2.2.2.8. A reformed own resource based on VAT

The HLGOR considers that the current value added tax (VAT) based own resource should be replaced: in its current form, it is unnecessarily complex, has the disadvantage of having no direct link to the citizens and does not bring added value compared to the GNI own resource in terms of fairness and transparency. It was introduced with the Own Resources Decision of 1970 as a second own resource given the insufficiency traditional own resources to finance the Communities' budget expenditures. The VAT-based own resource became then the main source of revenue as of 1979, covering around 50% of the EU expenditure.

VAT-based own resource contributions derive from the application of a call rate to Member States' VAT bases, set according to harmonised rules. The call rate was firstly fixed at 1% and later in the mid-80s raised to 1.4%. However, in the late 80s, this resource revealed itself to be insufficient to cover the financing needs and GNP was introduced in the financing system, as the balancing resource.

VAT bases of each Member State are capped, firstly at 55% of GNP and currently at 50% of GNI. The capping of the VAT base reflect the intention to remedy the regressive aspects of the VAT-based resource, which could be seen as penalising the less wealthy Member States with higher shares of consumption. Already in the 2000s, as GNI gained ground as a financing main resource, VAT-based own resource call rate was reduced progressively down to the current 0.3%.

The VAT-based own resource also served over time as a base for the creation of compensations to certain Member States whose financial contribution to the budget was considered to be an excessive budgetary burden. In the late 80s, a correction was granted to the United Kingdom in a form of a reduction to its VAT-based contribution. Already in the 2007-2013 financial period, a reduction to their VAT-based contribution was also introduced to Austria, Germany, the Netherlands and Sweden in a form of a lower VAT-based own resource call rate.

Currently, the VAT own resource is based on a statistical complex exercise created with the purpose of minimising distortions due to diverging VAT rates and structures in the Member States. The VAT bases are theoretically harmonised for the purpose of own resource calculations. This harmonised VAT base is calculated by dividing the total annual net corrected VAT revenue collected by each Member State by an estimation of the average rate applicable to the categories of taxable goods and services. This gives the intermediate VAT base.

The intermediate base is subsequently adjusted with negative or positive compensations in order to obtain a harmonised VAT base pursuant to the VAT Directive.

In addition to the complexity and non-transparency of the correction mechanisms and the harmonisation calculations just described, VAT-based national contributions also reveal a visibility constraint. VAT-based contributions to the EU financing are veiled in some Member States as they appear as expenditure in national budgets, which may give the impression that such payments are conditional on the vote of the national budgets and compete with national expenditures. This fact has no legal consequences but creates visibility and awareness breakdowns close to the national politics and citizens.

As for the financing capacity of the VAT resource, currently it is responsible for the financing of 12% of the EU overall expenditure. This share has changed substantially over the years mainly due to VAT-based own resource call rate reductions and to the increase in the overall volume of the EU budget. Nevertheless, the pattern and amount of the revenue stemming from this resource has been stable over recent years.

#### A reformed VAT own resource

Over time, the VAT-based own resource has revealed problems of complexity and non-transparency in the way it is determined, problems of sufficiency due to the decreasing share in the financing capacity and problems of visibility for European citizens and Member States. It has nevertheless also displayed strengths such as sustainability, stability, efficiency and fairness.

The Group would see two main approaches towards a reformed VAT own resource. The first one is similar to the Commission proposal of 2011, where a new VAT resource would derive from a simple application of a fixed EU rate in all Member States on the net value of supplies of goods and services, on the intra-EU acquisitions of goods and on imports of goods to which a standard VAT rate is applied in every Member State. At the time the proposal did not receive sufficient support, but the European Council of 7 and 8 February 2013 encouraged the Council to continue working on the issue. The stated objective was to make the VAT resource as simple and transparent as possible, to strengthen the link with EU VAT policy and actual VAT receipts, and to ensure equal treatment of taxpayers in all Member States. The European Council concluded that the new VAT-based own resource could replace the existing one, which would then be removed. This first possibility for a new design of a VAT-based own resource is therefore focussed on simplification, fairness and efficiency.

The second possibility regarding a new VAT own resource would be more focused on the tax harmonisation objective for VAT and on European added value. It would consist in applying the same fixed EU rate to a wider harmonised VAT base. The fixed call rate could be lower as the base would be broader, since it would include all goods, services and transactions independent of their VAT national rate. This possibility would not discriminate against any type of good or service by preventing it from entering a common base or by being excluded from it — contrary to the first possibility —, preventing national description on it.

## How does a reformed VAT own resource score?

**1. Equity/Fairness:** in the current system, equity is ensured by the reduction of the call rate of the VAT-based own resource for a group of Member States in order to balance its regressive nature. However, this provision aims at equity and fairness between Member States, not between EU taxpayers. Both possibilities for a new VAT-based own resource appeal to fairness between taxpayers over what consumption level is concerned. However, they do not take into account the level of consumption versus the level of income.

**2. Efficiency:** the current system applies a fixed call rate to all Member States that is currently at 0.3%. This provision proved to be simpler, more transparent and more efficient to calculate than the previous complex 'frozen' rate system. Nevertheless, calculation remains cumbersome for the establishment of the theoretical VAT base built on highly complex statistical sets of data which vary in each Member State. In addition, in the current system some Member States have achieved a reduction of the call rate and one Member State even had its right to a correction granted.

In the first possibility presented and in accordance with 2011 Commission's proposal, a simpler and less cumbersome system is suggested. Its base calculation would be:

- » the adjusted VAT receipts for the month;
- » the single EU-wide average proportion of VAT receipts accruing from standard-rated supplies to final consumption provided by the Commission;
- » their standard rate; and
- » the share determined for the new VAT own resource (1 or 2%);

The Commission would then have determined a single EU-wide average proportion of VAT receipts accruing from standard-rated supplies to final consumption, which are standard-rated in every Member State. This

calculation would exclude any artificial capping of the chargeable bases.

Regarding the second possibility, in addition to the data necessary for the calculation mentioned above, Member States would have to communicate the EU total VAT base including the goods and services subject to zero VAT rates and exemptions in order to apply a fixed rate to the overall base. This additional burden, since it would not be taxed to consumers and consequently not collected by national administrations, would have to be covered by Member States' budgets. Nevertheless, this contribution from the national budgets could serve as an incentive to Member States to reduce the share of VAT exemptions and zero and reduced rates, which is already an objective fixed in the European Semester.

**3. Sufficiency and Stability:** as far as sufficiency is concerned, the share of the revenue accruing from the VAT-based own resource would be fixed in all possibilities presented, by the call rate or the fixed rate applied to the VAT base, similarly to the present system.

Regarding stability, the pattern and amount of the revenue from the VAT-based own resource have been stable over the last years, at around 12% of the total own resources entered in the EU budget in the last five years, revealing that a VAT-based own resource is able to ensure a high predictability of receipts. It is considered a reliable source of revenue with limited volatility, which is fundamental for the stability of the collection of revenues and for EU financial autonomy.

**4. Transparency and Simplicity:** the current calculation of the theoretical VAT base can raise transparency questions as it is complex, statistically-based and far from the real VAT collected revenue. Both possibilities mentioned guarantee a considerably more transparent, understandable and predictable VAT resource. Both stem from simpler calculations on the basis of the most definite and easily obtained data available on the VAT receipts held by Member States. Both possibilities involve less corrections and compensations to be applied to VAT receipts. They can also play an important role in increasing the awareness of the costs of the EU for citizens (if EU and national VAT were to appear as separate taxes on invoices or receipts).

**5. Democratic accountability and budgetary discipline:** any new VAT-based own resource as part of the overall financing system of the EU budget would be approved by the Member States in accordance with their respective constitutional requirements, subject to European Parliament scrutiny, to the Court of Auditors audits and checks by the Commission. National parliaments would be also involved in the real VAT collected revenue for the national budgets.

**6. Focus on European added value:** the current VAT-based own resource is calculated in accordance with a common EU directive, although it remains a statistical construct. Both possibilities proposed would be closer to a genuine own resource, in line with TFEU provisions, and would probably be perceived to a lesser extent as a national contribution. The use of the actual VAT base in the calculation method, instead of the current theoretical VAT base, would have created a stronger link with EU policies, and probably increased the awareness of the costs of the EU for citizens. They could also play a part of a wider effort on VAT fight against fraud and VAT tax harmonisation in the EU.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** the VAT-based own resource is based on the national collection of real VAT, calculated by the national tax authorities in coordination with the national and European statistical authorities and checked and audited by the Commission. This calculation imposes high administrative costs, which are, however, already provided for and implemented both at national and European level. In the first possibility, since the VAT resource would stem from actual VAT proceeds, it would have a more cost-effective implementation since the national collection system is already in place and the calculation would be simplified, thereby reducing costs for both administrations. Under the second option, Member States would have to communicate additionally their VAT bases subject to zero rate and exemptions, similar to the current communication arrangement, and apply a fixed rate to the base value.

**8. Limit political transaction costs:** since VAT is collected under a legal and economic EU harmonised legal basis established already for several years, political transaction costs can be considered to be low in any of its possible forms.

### Overall assessment

VAT is the only tax already governed by EU law, and while further harmonisation of its base has stalled and even decreased over the years with the multiplication of exemptions requested by Member States, the recent VAT Action Plan launched by the Commission has put it back on track, in particular as part of a wider effort to fight against fraud. Annual estimates of VAT fraud are indeed higher than the annual EU budget itself. In 2013, the 'VAT gap' — the difference between the expected VAT revenue and VAT actually collected in Member States — was almost EUR 170 billion. Cross-border fraud alone is estimated to be responsible for a VAT revenue loss of around EUR 50 billion a year in the EU. At the same time, the current VAT system remains fragmented and creates significant administrative burdens, especially for SMEs and online companies.

A reformed VAT own resource would contribute to this wider effort to fight against fraud and to facilitate the life of European companies. It would also have political, legal and historical advantages over other possible own resources candidates of fiscal nature where harmonisation efforts are only beginning.

Overall, VAT is considered a reliable source of revenue with limited volatility, which is fundamental for the stability of the collection of revenues and for EU financial autonomy.

The implementation of the first possibility, in accordance with the Commission's 2011 proposal, i.e. the new VAT-based own resource, would have ensured a higher predictability of receipts. The Commission proposal to apply a rate of 1% to the standard VAT rate applied to the final consumption of goods and services estimated that the collected revenue could reach EUR 20.9 billion (2009 prices), taking into account the current degree of harmonisation of VAT rules between Member States, and EUR 50.4 billion with further harmonisation or the broadening of national VAT bases (for example the reduction of the scope of zero or reduced rates). Consequently, the implementation of the second possibility would provide even higher revenues, or the possibility to lower the fixed rate to be called by the EU.

Both possibilities for a direct application of a VAT fixed rate to all or to a given basket of goods and services would reduce inequalities, complexity, non-transparency and administrative costs. It would put an end to corrections and call rate reductions built on the current system reducing opacity of the VAT own resource.

The revision of the VAT-based own resource already has the support of the European Council, which called in February 2013 upon the Council to continue working on the Commission proposal, for a new own resource based on VAT to make it as simple and transparent as possible, to strengthen the link with EU VAT policy and actual VAT receipts, and to ensure equal treatment of taxpayers in all Member States. This shows interest for a future own resource based on VAT.

### 2.2.2.9. Seigniorage

Seigniorage is the central bank or government revenue made from issuing currency, especially the difference between the face value of circulating banknotes and coins and their production costs, as well as from central bank deposits. Inside the euro area (EA) this income is currently collected by the European Central Bank (ECB) and distributed among the national central banks of the EA Member States according to the ECB capital key (Article 32 ESCB Statute). It becomes part of central

banks' profits, whose use is regulated at Member State level. The largest share of these profits is then paid out to national treasuries, after deduction of operational and administrative costs, where it is generally accounted as budgetary revenue. Seigniorage had been analysed in the 2011 Commission report on the operation of the own resources system, but has not been the object of an actual legislative proposal.

## How does seigniorage score as an own resource?

**1. Equity/Fairness:** the distribution of income from seigniorage is based on a specific key: the ECB capital key, which reflects each country's share in the total population and gross domestic product of the EU and determines the share of each country to the ECB capital. However, only EA Member States pay their share in full, while non-EA Member States pay only a small fraction in order to contribute to the ECB's running costs. The ECB adjusts the shares every five years and whenever a new country joins the EU, ensuring a fair and regularly updated distribution.

**2. Efficiency:** the technical calculations for this revenue stream being in place, implementation could be relatively straightforward if this revenue source was to finance any EA future objective or policy. At the EU level, however, it would therefore require that an equivalent amount to be statistically built for non-EA Member States, or that they be treated in a differentiated manner, and thus probably increase the complexity in the system. For example, the share of the euro area seigniorage income in the GNI of EA Members would be calculated, the non-EA members would contribute an equal share of their GNI, but in order to determine the national contributions within this group of countries, the ECB capital key could be applied as distribution key.

**3. Sufficiency and Stability:** the total amount of income from seigniorage has been rather volatile in recent years, fluctuating in a range of about EUR 10 to 25 billion and coming in at the low end of the range most recently (EUR 10 billion per year would represent around 6 to 7% of the total EU budget). It could only play a role as an own resource combined with others at the EU level. Should it be envisaged for future EA purposes only if the idea of a EA budget or fiscal capacity takes form, its sufficiency and stability would have to be reassessed depending on the objectives and design of such budget or capacity.

**4. Transparency and Simplicity:** the administration of such a tax is simple as its revenue is already collected centrally. Collecting it as an own resource would not entail any additional burden. However, considering the own resources system as a whole, it could only apply

to the Member States of the EA and would require introducing differentiation in the treatment of EA members and non-members on the revenue side. In order to avoid more complexity in the own resources system, such revenue would thus be more suitable to finance specific EA purposes.

**5. Democratic accountability and budgetary discipline:** the whole European system of central banks is conceived so as to safeguard the ECB's independence from political influence. Seigniorage revenues are therefore a given and do not depend on budgetary decisions. The creation of a new own resource from seigniorage would not change this fact.

**6. Focus on European added value:** an own resource based on ECB seigniorage would have a direct link to a fully developed EU policy: the monetary union. In this sense it would have the characteristics of a real own resource. However, it would require adjustments in relation to non-Euro members. For this reason, it would probably be a better source of revenue for EA purposes, as explained above.

**7. Subsidiarity principle and fiscal sovereignty of Member States:** the subsidiarity principle would logically suggest that central banks profits are allocated at the EU level and not at the national level, as they stem from an integrated currency area where national sovereignty is fully shared at the EA level.

**8. Limit political transaction costs:** the highest political transaction costs, however, lie in the fact that a Treaty change would be needed as the allocation of seigniorage to national central banks is provided for in Protocol n°4 of the TFEU. In addition, it would have a direct impact on national budgets since they are currently the recipients of seigniorage income. Opposition of national central banks would be strong.

## Overall assessment

There is a fundamental economic rationale which would justify seigniorage revenues financing the EU future: it is fair and equitable, it is directly linked to a fully developed, sui generis European policy. These revenues are not simply the addition of what national revenues from printing money used to generate before the creation of the euro, they also result from the fact that the euro has become an international reserve currency, a status most national currencies did not have.<sup>42</sup> Such 'genuine' quality as an own resource, however, can only be legitimately seen in the context of the euro area. As the distribution of seigniorage income is governed by EU primary law, it would also probably entail, even in the EA context, a far-reaching policy package beyond EU financing considerations.

42. 'Seigniorage, its history, its present, and its future for the European Union', A.R. Leen, Archives of Economic History, Volume XXIII, No 1, January-June 2011, pp. 7-16.

## PART 3 — ADDITIONAL ELEMENTS FOR A PACKAGE DEAL

### 3.1. Take a second look at net balances

#### 3.1.1. Budgetary balances: methodological concepts, origin of the method, UK correction, Fontainebleau logic

The EU budget was never conceived to be primarily a system of fiscal equalisation or redistribution between Member States. Its main purpose has always been to finance common costs and operational expenditure linked to Treaty obligations and common policies, in particular the common agricultural and cohesion policy. The nomenclature of the general budget reflects that: budgetary spending is not allotted to Member States but to policy areas.

However, this rationale was turned upside down with the need to address the United Kingdom's 'budgetary imbalances',<sup>43</sup> as Member States agreed at the European Council of Fontainebleau in 1984. It became necessary to measure the precise contribution to the budget by Member State and the precise returns from the budget back to each Member State. In order to do so, all expenditure had to be 'allocated' in one way or another to one specific Member State, even expenditure with high European added value content. On the income side, what is legally an own resource belonging to the EU has to be considered as a national contribution. The emerging difference between the contribution and allocation results in a 'net balance' position. This balance can be expressed in amount or in a percentage of the Member State's GNI.

A clear split thus emerged from this calculation between 'net contributors' and 'net receivers',<sup>44</sup> underpinned by numerical indicators. Over time, net balances have become the overarching reference in any budgetary negotiation.

Two types of net balances are calculated today: the operating budgetary balances (OBB) and the UK net balance.<sup>46</sup> The 'UK-net balance' is used to calculate the UK rebate every year and is therefore the only definition of net balance calculations laid down in EU legislation. In its annual financial report the Commission uses 'operating budgetary balances', which exclude administrative expenditure.<sup>45</sup>

*The current calculation of net balances leads to the perception of the EU budget as a zero-sum game. It ignores the very notion of added value.*

From the point of view of the present report, and in particular the focus on added value, these calculations present a major drawback: they simply ignore the notion of added value. Their purpose is only to show the relative burden sharing of EU financing between Member States. Hence, both the operating budgetary balance and the UK net balance are built on the premise that the sum of all Member States' net balances equals zero.

Any allocated expenditure from the EU budget therefore appears to be either a cost or a benefit for a given Member State, whether or not such expenditure benefits several or all Member States, or addresses a European public good. As an example, the expenditure voted to reinforce the protection of EU external borders is allocated to the countries where these borders are located, as if the protection of these borders was to their benefit only and not the benefit of the Union as a whole.

The issue would not be problematic if the annually published figures for the net balances were not used for what they were not conceived to be: a proxy for 'cost-benefit' assessments, an indicator of solidarity or even a measurement of excessive budgetary burden. But in practice, they are; and crucially so within the context of budgetary negotiations.

43. More detailed history of the 'budgetary imbalances of the UK' and the ways to address them are elaborated elsewhere, see for example European Union, Public Finance, 5th edition.

44. The fact that 'net receivers' and 'net beneficiaries' are normally used as synonyms, illustrates the dilemma at hand.

45. In the European Council of March 1999 in Berlin it was agreed that 'when referring to budgetary imbalances, the Commission, for presentational purposes, will base itself on operational expenditure'.

46. They artificially adjust the level of national contributions to equal the total of allocated expenditures.

Both sides of the equation should be scrutinised: on the expenditure side, the ‘allocation’ of every item of expenditure suggests that every euro benefits only one Member State and is a cost to all others. By definition, not a single euro is considered as being beneficial to several or all Member States, or spent on European added value. Additional indicators should therefore be developed to show that a share of expenditure at least, or simply regulation at the supranational level, benefits all Member States. As analysed in point 1.3.2., it seems that this share has increased overtime, in particular in the last two decades.

On the revenue side, the confusion of ‘national contributions’ with ‘own resources’, which translates in many different manners in national budgets, is problematic because it prevents meaningful and transparent comparisons (see point 1.2.1.2.).

### 3.1.2. How are net balances deceptive from the point of view of European added value

In a text-book system of fiscal transfers, net balances, by definition, are meant to be a ‘zero-sum’ construction. In the reality of the EU budget, however, there are several factors which make the situation more nuanced: on the spending side, as mentioned, there are administrative costs and expenditure allocated to third countries which do not enter in the calculation. Expenditure items which benefit several countries are allocated to one Member State or artificially split up.

On the revenue side, custom duties are not taken into account (they are ‘genuine’ own resources, not attributable to individual Member States in principle), just as other revenue. The resulting, adjusted, artificial accounting figures are not necessarily a faithful reflection of the underlying economic reality.

In order to show how deceptive this ‘zero-sum’ construction of the operating budgetary balances (OBB) can become, two scenarios are envisaged below, on the basis of aggregate real data (average of 2007-2013). They explore, as an experiment, if in the present system, configurations are possible where all Member States could be net recipients, or net contributors.

In scenario 1, it is assumed that there are unusually high amounts of custom duties and other revenue in a given year: 60% of the total revenues of the budget — instead of 20% on average for 2007-2013.

These revenues are assumed to be fully collected and budgeted and are, correctly, not considered as national contributions. The amount covered by VAT-based and GNI-based own resources therefore represents only 40% of the total revenue.

Intuition would lead us to think that in such a year where a very large share of the budget is financed via real own resources, almost all Member States should surely become net recipients and should have a positive balance. However, results of the calculations shown in Table A suggest that this is not the case: save some impact on the UK calculation, each Member State has exactly the same net balance, in percentage and in amount (which is thus purely notional). This naturally results from the OBB method: lower amounts called national contributions are artificially ‘expanded’ to equal the total amount of allocated expenditure.

One conclusion from this experiment is that a higher amount of genuine or real own resources would not per se change the zero-sum game construction.

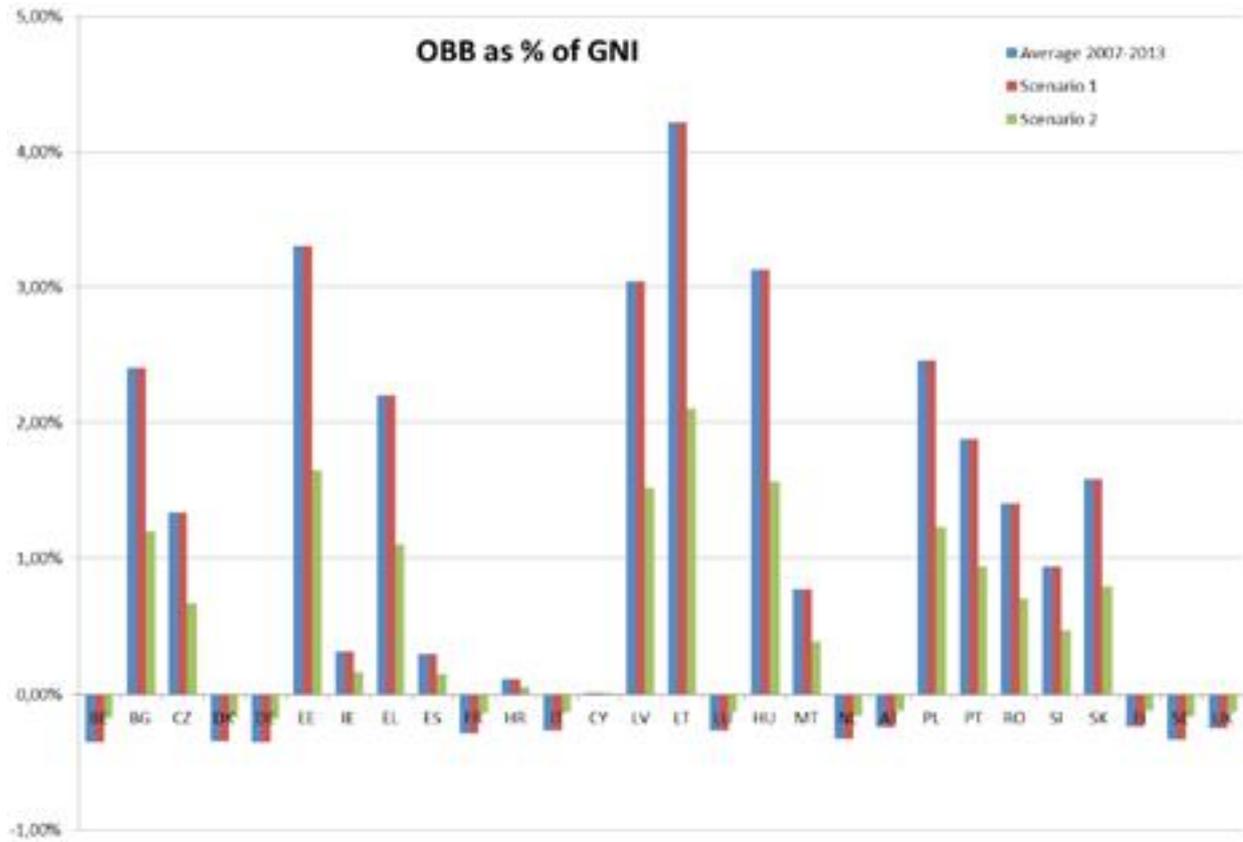
In scenario 2, it is assumed that in a given, very exceptional year, expenditure allocated to Member States is reduced by 50% and the difference is spent in favour of third countries (for example for development cooperation and humanitarian aid).

It could be expected that, since most of EU expenditure benefits third countries, all Member States would become net contributors. Yet again, the result from the OBB method is counter-intuitive: in such case, the national contributions would be adjusted downwards to fit the level of allocated expenditures. The consequence on net balances would be a proportional reduction both in absolute and percentage terms. Net contributors remain net contributors, and net beneficiaries remain net beneficiaries, but smaller ones. The ‘zero-sum’ configuration is maintained, but is confined to the now smaller part of allocated expenditure.

The table below shows the resulting OBB as a percentage of GNI for these two scenarios, compared to a baseline of the average for 2007-2013.

These two scenarios should in the first instance be understood as a plea to take the annually published OBB figures, and the net balances from which they are derived for what they are: mere indicators, not measurements of costs or benefits to be taken at face value. Operating budgetary balances show the relationship between a Member State’s share of total allocated EU operating expenditure and its share of ‘national contributions’.<sup>47</sup>

47. As the annual financial report recalls: Member States’ operating budgetary balances are calculated based on data on the allocation of EU expenditure by Member State and on Member States’ contributions to the EU budget. It is, however, important to point out that estimating operating budgetary balances is merely an accounting exercise that shows certain financial costs and benefits derived from the EU by each Member State. Furthermore, this accounting allocation is non exhaustive and gives no indication of the many other benefits arising from EU policies such as those relating to the single market and economic integration, not to mention political stability and security.



*Recent trends of the EU budget such as an increased focus on added value cannot be taken into account by net balances calculations.*

To sum up: the elements of EU budget expenditure which have, over recent years, brought increased European added value, or which favour recipients other than 'traditional' net beneficiaries, are largely ignored by the current methodology. In other terms, this calculation implicitly still considers the EU budget as a simple grant distribution tool transferring public money from one country to another, and overlooks its role in the mobilisation of private investments or its cross-border and multiplying effect.

Furthermore, an accounting system with a 'zero-sum' assumption can hardly capture the dynamic impact of investment flows stemming from the financial instruments embedded in and underpinned by the EU budget.

The analysis of the impact of financial instruments in point 1.3.2. shows that they primarily benefit the most developed areas of the Union because they have been designed precisely to counter suboptimal investment situations wherever they arise, not to favour regions that are catching up. On the other hand, the added value and cross-border economic spill over in the richer regions will indirectly benefit the entire single market.

What is prone to criticism is of course not the viability of the financial instruments themselves. It is the fact that the beneficiaries of these investments remain hidden from the net balance approach, despite the fact that they are primarily countries dissatisfied with their net balance position, which regularly quote the operating budgetary balances as a measure of their 'solidarity' or as a baseline for the 'excessive burden' that EU budget financing imposes upon them. In the light of the above however, these figures should be interpreted with great care, and should certainly not be the only indicator taken into account in budgetary negotiations.

The operating budgetary balance of each Member State is calculated as the difference between the operating expenditure (excluding administration) (1) allocated to each Member State and the adjusted 'national contribution' (2) of each Member State as follows: (1) In accordance with point 75 of the conclusions of the 1999 European Council in Berlin: 'When referring to budgetary imbalances, the Commission, for presentational purposes, will base itself on operating expenditure. (2) As in the case of the calculation of the UK correction, it is not the actual 'national contribution' of Member States (i.e. own resources payments, excluding traditional own resources (TORs), e.g. customs duties and sugar levies) but the related allocation key, i.e. each Member State's share of total 'national contributions', that is used for the calculation of operating budgetary balances. Total 'national contributions' are adjusted to equal total EU allocated operating expenditure, so that operating budgetary balances sum to zero. TORs are not included in the calculation of net balances. Since TORs are a direct result of the application of common policies (such as the common agricultural policy and customs union), they are considered to be pure EU revenue rather than 'national contributions'. Furthermore, the economic agent bearing the burden of the customs duty imposed is not always a resident of the Member States collecting the duty.

*Net balances published annually should be considered as mere indicators of the relative financing position of a Member State compared to the others. It should not be the only measurement of costs and benefits of EU membership.*

### 3.1.3. The ‘default’ negotiating approach by Member States

In the context of budgetary and MFF negotiations, observers and participants testify that, as a rule, Member States’ prime objective is to maximise the returns from the EU budget, preferably by means of ‘pre-allocated envelopes’, and to minimise their respective share of national contributions going into the EU budget. Member States consider this to be in their best interest.

The struggle to maximise cohesion envelopes, to improve the endowment of those programmes with traditionally high reflows to one’s own economic actors and strong sectors or the fervour with which budgetary corrections are pursued may seem rational in a traditional context of negotiators seeking to maximise benefits and minimise costs.

It reveals however, the lack — or the lack of recognition — of the added value that comes with spending programmes which are designed to underpin common European objectives and bring advantages, at least indirectly, to the entire single market.

*Policies which would benefit all EU citizens and provide more added value (such as internal and external security, the fight against climate change, etc.) are not ‘attractive’ in terms of net balances.*

One corollary of this approach is the comparatively weak position of the centrally managed, non-pre-allocated programmes under MFF Heading 1a (Competitiveness for Jobs and Growth) and Heading 4 (Global Europe, external spending ‘allocated’ to third countries). Budget lines under these headings present ‘soft targets’ for budget cuts, despite their often manifest added value — while agriculture and cohesion programmes are often ring-fenced and shielded from reductions in the annual and multiannual negotiations in Council. Similarly, the insistence by some Member States to keep the MFF ceilings and especially the level of payment

appropriations as low as possible is linked to the wish to prevent negative budgetary balances reaching a certain level deemed unacceptable. This has led to a multitude of correction mechanisms and ad hoc ‘gifts’ on the spending side resulting from the MFF negotiations, considered as necessary to achieve an equilibrium of projected net balances.

Such observations are not meant to make a caricature of Member States’ negotiation behaviour. After all, many of them do eventually accept negative balances (at least up to a certain degree), which confirms that there is an appreciation of more indirect benefits.

Still, the threshold for considering the negative balances as an ‘excessive’ budgetary burden under the present conditions remains rather low. In order to change this perception and the underlying reality, changes are necessary on the expenditure side as well as on the revenue side.

### 3.1.4. Net balances after the UK withdrawal

When the UK withdraws from the EU, the UK correction will become obsolete. This will also be the case for what are called the ‘rebates on the rebate’, i.e. the reductions which Germany, Austria, the Netherlands and Sweden benefit from the financing of the UK correction. As a consequence, the largest part of the regressive effects of the ‘per capita burden’<sup>48</sup> on the revenue side which are due to the UK correction will also disappear — all else being equal.

In this context, other financing issues which are closely connected to the UK correction, and which have been so far difficult to reform for this reason, should be re-examined. This is the case of the statistical VAT-based own resource (including its capping), which has little to no advantage over the GNI-based contribution. The Commission has presented several proposals to abolish or reform the VAT-based own resource over the years — the last once in 2011 — but they were all rejected, primarily because they would have required modifying the calculation method of the UK correction as well. If this is no longer the case, there will be little appetite to maintain this least cherished own resource in the future.

Furthermore, and in close connection with the net balance discussion, once there is no longer a need to calculate the UK correction, the Commission will have no other independent legal base which would require

48. See footnote 9, *Ibid.*, pp. 23-24.

the ‘allocation’ of expenditure as it is currently done in the operating budgetary balance calculation. This should be an opportunity for the institutions to devise a more appropriate method to assess the costs and benefits of the EU and to assess the relevance of the net balance concept. In this perspective, the European added value of EU policies should not be left out, or the defects and omissions of the current calculations will remain and the perception of the EU as a zero-sum game will continue unabated.

**RECOMMENDATION 7 – Corrections and rebates.**

*Withdrawal of the UK from the EU entails the discontinuation of the UK correction mechanism and the related ‘rebates on rebate’. This in turn makes much of the rationale for the present statistical VAT-based own resource superfluous.*

### 3.1.5. Towards a better assessment of what Member States pay to the EU budget and receive from it

The reflections concerning net balances calculations should not be dismissed because of the prevalence of these figures in the debate about equity and fair burden sharing in relation to the EU budget.

It should therefore be systematically clarified that the following elements of European added value are not captured by the operating budgetary balance methodology, such as:

- » collective, cross border and other indirect benefits arising from budgetary interventions and the supply and demand effects which they trigger in countries other than the immediate recipient of an allocation;
- » synergies and global economies of scale resulting from European cooperation at all levels instead of financing 28 separate policies or programmes;
- » ‘multiplication effects’ resulting from the investment flows leveraged through the increased use of financial instruments and guarantee schemes underpinned by EU budget support.

The methodology currently used to calculate net balances shows that neither the increase of public-good-type expenditure in the budget, nor the

introduction of genuine own resources per se would lead to very different operating budgetary balances. The focus of Member States to maximise reflows and ‘pre-allocations’, and the ‘common pool’ problem would persist, regardless of the composition of the income side.

If the juste retour dilemma and the related ‘zero-sum’ game perception are to be overcome effectively, reforms would best be initiated on three fronts simultaneously: the expenditure side, the revenue composition and the methodology of calculating balances. More specifically, the Group recommends:

- » Focussing on EU policies which can bring the most added value
- » introducing alternative revenue sources which are not perceived as national contributions but rather as resources directly linked to the European dimension, and
- » complementing the budgetary net balance calculations with more inclusive cost-benefit analyses so that the benefits of policies and public goods with manifest European added value is better reflected. The net budgetary balance methodology should not artificially re-construct the calculations as if all spending were allocated to individual recipients and made up of national contributions.

The Group also recognises that factual data are incomplete and recommends further analysis to calculate the secondary economic effects and financial flows triggered by EU budget interventions in Member States, including investments linked to EU financial instruments. This should give a more accurate view of the costs and benefits per Member State and help show that one Member State’s gain is not inevitably at the others’ cost. If the next generation of spending programmes under the new Multiannual Financial Framework is to meet the growing expectations, the challenge lies in overcoming this impasse.

**RECOMMENDATION 6 – Aim at a more comprehensive and accurate notion of ‘costs’, ‘benefits’ and ‘net balances’**

**RECOMMENDATION 7 – Corrections and rebates**

### 3.2. A more subtle way forward: is differentiation possible for EU revenue?

There has long been some measure of differentiated integration, in particular since the introduction in the Maastricht Treaty of actual opt-outs for the UK and Denmark with respect to Economic and Monetary Union, and for the UK with respect to social policy. Differentiation covers many different meanings and even reflects the different views on what the EU is about. It came to prominence in the debates over institutional reform in mid-1990s, together with the perspective of enlargement to an unprecedented number of countries, as a way forward to sustain the objective of 'an ever closer Union' in the midst of increasing diversity. The current Treaty provision allowing enhanced cooperation is based on this idea. Since the great financial and economic crisis of 2008, differentiation has been accelerating, in particular to answer pressing needs which could not be dealt with under the MFF.

*There are two main degrees of differentiation: multi-speed integration and variable geometry (or à la carte). All have consequences for and can be applied to the revenue*

The different degrees of differentiation were developed conceptually over 20 years ago, notably in the landmark and controversial paper by Karl Lamers and Wolfgang Schäuble, and in the classification presented by Alexander Stubb. These analyses are useful to understand the underlying political forces driving policy.

To grossly simplify, there are two main types of differentiated integration: the first one is referred to as 'multi-speed' integration, the second one as variable geometry or à la carte. Multi-speed integration refers to a policy which is pursued by a core group of Member States which are both able and willing to go further, with the underlying assumption that other Member States will follow later. Variable geometry or à la carte refers to a permanent differentiated integration between a core and less integrated Member States, where the latter chose not to participate to specific policies.

While it has become a generally accepted solution that forward-looking policies which were not mature enough to be endorsed at the EU level could be adopted by a coalition of the willing, both types of differentiated integration coexist in today's EU. This naturally has consequences on a wide range of institutional, political and budgetary issues, including on the revenue side.

The table enclosed below shows the different types of differentiation that are possible on the revenue side in general, with respect to the policy underlying the own resources base (e.g. opt-outs, enhanced cooperation) and with respect to use of the revenue (universality/earmarking).

## The mapping of variable geometry of EU Revenue: differentiation in the sourcing and use of own resources and other revenue

		Legal framework of revenue / Degree of unity				
		Same for <b>all</b> MS - tax-based OR with all MS taking part in the 'base' - national contributions	Enhanced cooperation or permanent structured cooperation	Opt-outs in certain policies	Other revenue (mostly direct proceeds from economic actors)	A budget for the euro area
<b>Use / Destination of the Revenue / Degree of Universality</b>	General, universal revenue, fungible with GNI-based OR	<i>ORD and MFF</i>	<i>Next ORD and MFF (new OR for participating MS, GNI-based for non-participating MS (ex: FTT))</i>	<i>ORD and MFF, with reimbursements for MS having an opt-out</i>	<i>Secondary legislation (new generation of EU programmes)</i>	
	Earmarked revenue (unlinked to policy)	<i>Next ORD, for extra flexibility, reserves or a specific heading, e.g. fuel tax for migration policy</i>	<i>Combinations possible in principle</i>		<i>Extra flexibility or general reserve</i>	<i>General financing of the euro area fiscal capacity or budget</i>
	Earmarked revenue (with 'inherent policy link')	<i>Next ORD, for visibility and political legitimacy (ex: a CO<sub>2</sub>-tax for climate action)</i>	<i>Combinations possible in principle</i>		<i>Extra flexibility or reserve for specific policies (ex: ETS for climate action, travel authorisation fees for border management...)</i>	<i>Ad hoc financing (ex: FTT or FAT-type proceeds for Banking Union)</i>
	Extra-budgetary, Trust Funds	<i>Outside ORD and MFF (ex: EDF, national contributions to Facility for Refugees in Turkey)</i>	<i>- Ad-hoc national contributions - ad-hoc source of revenue (ex: fuel tax for migration policy, FTT for development aid (Tobin tax logic))</i>	<i>Outside ORD and MFF (ex: Schengen, defence...)</i>	<i>Fees for self-financing agencies</i>	<i>Fiscal capacity outside the EU budget</i>

The various forms of differentiation identified in the table, whether they are currently allowed or could be in the future, do not have the same impact on the revenue side. The point of non-differentiation is expressed in the upper-left case and summarises the main features of the financing system as provided for in the Treaty: all Member States contribute to the EU budget via the own resources, which in turn help finance all EU expenditure.

Any new own resource introduced in the future would therefore reduce the residual GNI-based own resource. Any form of differentiation should be considered as a derogation from this general principle of universality and, as such, be justified.

The multiple crises faced by the Union in recent years have increased the pressure to intervene either in areas other than its core business, or according to innovative instruments outside its well-established rules and procedures. The refugee crisis in particular has put in evidence the strain put on the EU budget and the limits of the current MFF, where the margins of manoeuvre are being stretched to their maximum to face the additional needs.

In response to the crisis, some measures are financed within the current MFF and therefore via the EU own resources, such as the significant top-up of Heading 3 'Security and Citizenship' in the 2016 Budget (to EUR

4.05 billion from EUR 2.52 billion in 2015), which will be covered by the Flexibility instrument.

## 3.2.1. Trust funds and similar instruments opened to all Member States

Other responses to the refugee crisis, like trust funds, include some differentiation in the sense that additional contributions from Member States are possible on top of the financing planned from the EU budget. This is the case of the Madad Fund, created in December 2014, to respond primarily to the needs of Syrian refugees in neighbouring countries and help the communities hosting them. The Madad Fund allows the pooling of financing from existing EU instruments from the external heading of the MFF (Heading 4 'Global Europe').

As a dedicated trust fund, it can also pool funding from third donors, including additional contributions from EU Member States on a voluntary basis. The Refugee Facility for Turkey also comprises some differentiation: EUR 1 billion to be financed from the EU budget for the years 2016 and 2017, while the other EUR 2 billion are to be financed from national contributions.

*Trust funds can provide a pragmatic answer to a specific need but are not suitable to implement long-term policies.*

Such differentiated arrangements provide a pragmatic and visible answer to an identified problem, or to the budgetary needs arising from new responsibilities that European leaders — gathered in the European Council — have entrusted to the Union (Juncker Plan, migration policy, security policy, follow-up of the COP21 and the climate change negotiations).

They make the EU budget more versatile and more efficient if the pooling of funds allows for economies of scale and synergies. They also allow increased cooperation between Member States which would otherwise not be possible.

Unsurprisingly, however, such differentiation normally implies a trade-off between the efficiency of decisions, the versatility of the EU budget on the one hand and the simplicity, equity and democratic accountability of the overall system on the other. The creation of ad hoc funds or instruments parallel to the EU budget obviously increases the complexity of the EU budget (see Annex IV), but can also render its implementation

more difficult: it notably remains to be seen whether trust funds do mobilise sufficient additional voluntary contributions, and if the uncertainty attached to these has an impact on other strategic and long-term policy planning.

*Further differentiation should be subject to proper parliamentary scrutiny.*

Finally, the most salient criticism towards differentiation as enacted in the examples above concerns their ad hoc governance and different control procedures. Trust funds are generally managed by a board of trustees representing the donors, and are therefore not submitted to the democratic control and scrutiny of the European Parliament like similar spending implemented under the responsibility of the Commission. The European Parliament has only the power to control the part of the financing coming from the EU budget — and hence financed from the own resources. While it can be assumed that national parliaments are empowered to control and scrutinise the relevant national contribution to an EU trust fund, there is no clear and established coordination between the national and European levels which can guarantee that parliamentary scrutiny applies to a trust fund in its entirety and in comparable manner to other similar instruments, at least today.

If such instruments were to remain in place or be developed in the future, and in particular if EU trust funds were made available also for internal EU policies (as is provided for under the current revision of the Financial Regulation), the issue of democratic accountability would need to be addressed in a comprehensive and equitable manner.

Should that be the case, the channelling of new European source of financing could be envisaged as well. On several occasions already, calls to find new means to finance 'unexpected' events have been made, such as an exceptional tax to finance the refugee crisis or the redirecting of cohesion funds to be used to this purpose.

Due to the current constraints on EU spending, finding new ways of financing may seem easier than revising the current 2014-2020 MFF, in particular because the payment ceiling covered by the own resources has become an 'untouchable' figure in some capitals. In other words, it may appear more appealing politically to agree to 'current own resources + additional financing', than to agree to 'more own resources'. This would correspond to what is described in the table above as earmarked revenue: Member States would contribute

(voluntarily or according to a key agreed in advance) to top up particular programmes or budget lines.

If the own resource decision itself were to allow the financing of a (new) policy via earmarked revenue — for example a carbon tax to finance new initiatives in relation to a low carbon economy — this would be a very significant departure from the principle of universality and the current own resources system, and could also raise equity issues between Member States. But it could also enhance the legitimacy and visibility of EU spending. If not all Member States can agree to such configuration, enhanced cooperation or permanent structured cooperation could provide ways forward.

*RECOMMENDATION 9 – Allow for a certain degree of differentiation.*

### 3.2.2. Enhanced cooperation

Enhanced cooperation is a form of differentiation provided for in Article 20(1) TEU enabling a group of willing Member States to go forward in any of the Union's non-exclusive competence areas, i.e. areas in which competences are shared with Member States, as defined in Article 4 TFEU.<sup>49</sup> It establishes that 'Member States which wish to establish enhanced cooperation between themselves within the framework of the Union's non-exclusive competences may make use of its institutions and exercise those competences by applying the relevant provisions of the Treaties [...] enhanced cooperation shall aim to further the objectives of the Union, protect its interests and reinforce its integration process'.

The enhanced cooperation launched to introduce the financial transaction tax (FTT) is an example in agreement with this provision. After the attempt to introduce an FTT for EU-28 failed, a group of Member States willing to further integrate in the financial taxation area decided to go ahead under enhanced cooperation. The main objectives of this process are to avoid fragmentation and non-coordination of taxation in the single market for financial services, to ensure a fair contribution of financial institutions in the aftermath of the financial crisis and to create disincentives for transactions which do not improve the efficiency of financial markets.

As of today, 10 countries belonging to the euro area are on the verge of reaching an agreement to introduce an

FTT in their national tax system. However, the possibility of using the proceeds of this tax to finance the EU budget, as an own resource or not, was put aside very early on. Whether such possibility can be envisaged to finance a future euro area fiscal facility or budget remains to be seen as well, despite the FTT being a good candidate to finance the European rather than the national level of spending (see points 2.2.2.6. and 3.2).

*Enhanced cooperation between a coalition of front-runners is only possible in areas of non-exclusive competences of the Union.*

Other initiatives could be undertaken in the areas of non-exclusive competences of the Union under enhanced cooperation, as long as they would serve the purposes of Article 20(1) TEU to further the objectives of the Union, protect its interests and reinforce its integration process. They would also have to respect the competences, rights and obligations of non-participating Member States.

Interestingly, the budgetary impact of enhanced cooperation is already delineated in Article 332 TFEU: the costs resulting from the implementation of enhanced cooperation are to be borne by the participating Member States, save the administrative costs borne by the institutions, which cannot be split and remain covered by the EU budget.

*New streams of revenue stemming from policies under enhanced cooperation could be accommodated as assigned revenue or own resources.*

It is also conceivable that certain policies implemented under enhanced cooperation generate a new stream of revenue. In such case, participating Member States could agree to make the proceeds, or parts thereof, available for the EU budget.

This could take the form of assigned revenue, earmarked for specific expenditure items or programmes which, in turn, ideally, would benefit the participating Member States. The areas of common security, the Schengen system or even defence spring to mind. The participating Member States in the financing of such areas would also

49. In accordance with Article 4 TFEU, shared competences between the EU and its Member States are: the internal market, social policy, economic, social and territorial cohesion, agriculture and fisheries (excluding marine biological resources), environment, consumer protection, transport, trans-European networks, energy, freedom, security and justice and common safety concerns in public health matters. By contrast, Article 3 TFEU lists the exclusive competences of the EU for which enhanced cooperation is not possible: custom duties, competition rules concerning the functioning of the internal market, monetary policy for the Member States whose currency is the euro, conservation of marine biological resources under the common fisheries policy, common commercial policy and international agreements when provided for in a legislative act of the Union.

be those eligible to the relevant expenditure scheme. Such an arrangement can be based on secondary legislation. Assigned revenue is, as a rule, additional to funding based on authorised appropriations in the annual budgetary procedure, outside the MFF and outside the own resources system.

Theoretically, it could also be defined as general revenue and hence lead to a reduction of the total GNI-based own resources, although it seems improbable that participating Member States would wish to share these revenues with non-participating Member States.

Alternatively, all Member States could decide at unanimity and through the Own Resources Decision to take into account the revenues stemming from enhanced cooperation, fully or in part. Such revenues would then be treated as own resources for the Member States participating in the enhanced cooperation only, and would reduce their GNI-based contributions. The non-participating Member States would pay their normal share of GNI-based contributions. This would induce a differentiation in the uniform rate applied to GNI, but would preserve the universality of the budget: the revenues concerned would not be earmarked and would not give rise to appropriations outside the budget procedure or the MFF.

Differentiation on the revenue side is therefore indirectly introduced via enhanced cooperation, even if the underlying idea remains that such differentiation should remain open to all non-participating Member States so that they can participate once prepared or willing to do so.

The provisions on enhanced cooperation provide protection for both participating and non-participating Member States and limit the risks in terms of fairness or democratic accountability. However, when applied to taxation cooperation, enhanced cooperation requires finding a difficult balance to avoid economic risks such as distortion, discrimination and potential incentive to non-harmonisation between participating and non-participating Member States.

### 3.2.3. Opt-outs

Opting-out clauses are laid down in various protocols annexed to the treaties and concern, on the one hand, the UK and Denmark as regards the third stage of Economic and Monetary Union (EMU) i.e. the adoption of the euro, and on the other hand the UK, Ireland and Denmark in the area of freedom, security and justice.

These protocols exempt these Member States from taking part in these policies, to different degrees. It is the closer example to 'à la carte' differentiation.

The budgetary impact in this case is very similar to the one under enhanced cooperation: these Member States bear no financial consequences of the policies from which they have opted out, other than the administrative costs borne by the institutions. In practice, the impact of the opting-out clauses is calculated annually: the share of opted-out countries is financed by the remaining Member States and reimbursed to them at the end of the year.

This system entails a complex cost estimation exercise and would be extremely inefficient to apply in a broader range of policies. In addition, as it requires pre-financing of expenditure by opted-out Member States which is only reimbursed to them at year-end, it would certainly represent a heavy financial burden for them if used in a wider context.

### 3.2.4. Corrections and rebates

While the examples above concern differentiation on the expenditure side which have consequences on the financing side, there are also several corrections and rebates currently applicable directly on the financing side of the EU budget. They have been facing criticism for their complexity, non-transparency and for being the result of political bargaining during budgetary negotiations.

Previous reform attempts have failed to modify them or reduce their number, as explained in the First Assessment Report. The way these corrections are currently designed and negotiated reinforce the perception that they merely serve the purpose of achieving unanimity of the MFF rather than bring more equity to the overall system. They result from the national perception of net contributions to the EU budget based on the 'operating budgetary balances', which is the only indicator currently used by Member States to negotiate their contribution to the EU, as explained at length in point 3.1.

The most emblematic correction in the own resources system is the 'UK rebate', which has been in force since 1986 and introduced with some adjustments in the Own Resources Decision adopted in 1988, with unlimited duration.<sup>50</sup> However, this provision should become obsolete once the UK withdraws from the EU, consequently ending this correction and the other rebates linked to it. The EU therefore has the unique

50. For a more detailed historical account, see chapters 2 and 3 of the publication *European Union Public Finance*, European Commission, 5th Edition: [http://ec.europa.eu/budget/news/article\\_en.cfm?id=201501061636](http://ec.europa.eu/budget/news/article_en.cfm?id=201501061636)

opportunity to reevaluate the need and the basis which currently support the justification of rebates. If the EU budget is geared towards policies with more European added value in the future, as this present report argues it should, the need for corrections on the revenue side should actually disappear.

*RECOMMENDATION 7 – Corrections and rebates*

### 3.2.5. Overall assessment on differentiation

What would be the long-term consequences for the EU budget? As a general remark, the different types of differentiation are not as watertight as we might think. A clear differentiated integration process can evolve with time towards more integration into a common policy (Schengen). In the case of the euro area, even differentiation enshrined in the Treaty via the opt-outs was not sufficient to address the pressure of the crisis and prevent additional intergovernmental arrangements outside the Treaty. Points 3.3. and 3.4. below will address in more detail the issues linked to other revenues and the euro area. As an example to the contrary, intergovernmental agreements can also become more integrated into common EU policies, such as the Treaty of Brussels creating the Western European Union, whose main provisions have been included in the Common Security and Defence Policy of the TEU.

The variety of the examples presented above should allow for a pragmatic approach on differentiation, even as concerns its financing aspect. The rules need to be clear as regards the respective rights and obligations of both participating and non-participating Member States, and the democratic accountability of any initiative undertaken under differentiated cooperation needs to be clarified — and sometimes established —. Differentiation remains nonetheless a very useful tool when the needs and objectives of a group of Member States, or when the financing of a new initiative, cannot be assumed by the EU as a whole or financed via the EU budget. Depending on the nature of the hurdle, different types of differentiation can be used, with varied consequences for the EU budget, which may become more versatile and responsive, but also more complex.

### 3.3. An example of differentiation: the idea of a euro area budget

The debate on differentiation flourished together with the perspective for intensified integration and cooperation in areas closer to the core of sovereignty of Member States such as home affairs, external policy and defence. Since the big financial and economic crisis of 2008, however, it has also increasingly been referred to as a way forward to encompass the economic aspects of European Monetary Union, for those Member States which have adopted the euro as their currency, in order to overcome the weaknesses embedded in the Treaty and pave the way for a fully-functioning euro area. These economic aspects include in particular a capacity to tackle the specific characteristics of a monetary union, such as the need for automatic stabilisers, and the fiscal and budgetary policies of the participating Member States.

*The financing aspect of a euro area budget will need to be adjusted depending on what such budget should be used for.*

The idea of a euro area budget should be seen in this context, although there is no clear understanding — nor agreement between euro area members — on what such a budget should be used for. It is therefore difficult to envisage how such budget should be financed if its purpose and its foreseeable size are not delimited. However some assumptions can be made and guidance can be provided in order to define its main features.

In general, economists and political figures alike refer to three main functions for a euro area budget:

1. macroeconomic stabilisation and short term growth;
2. competitiveness and long-term growth through the financing of common projects;
3. crisis management.

A budget authority, whether created within the EU institutional framework or via a separate authority such a European treasury, would have to be created to manage the expenditure and revenue of such budget, and ensure appropriate accountability and governance.

As of today, only the function of crisis management in the euro area has been addressed with, on the one hand, the EFSM/EFSF/ESM<sup>51</sup> vehicles, and on the

51. The EFSM (European Financial Stabilisation Mechanism) provides financial assistance to EU Member States in financial difficulties. It relies on funds raised by the Commission on the financial markets under an implicit EU budget guarantee. The EFSF (European Financial Stability Facility) was created as a temporary crisis resolution mechanism for the euro area Member States and has provided financial assistance to Ireland, Portugal and Greece through the issuance of bonds and other debt instruments on capital markets. It was then replaced by the European Stability Mechanism (ESM), a permanent rescue mechanism endowed with an increased lending capacity (up to EUR 500 billion) for responding to new requests for financial assistance by euro area Member States. The ESM has provided loans to Spain, Cyprus and Greece.

other hand, the banking union, although it is not fully operational yet and has been set up through separate intergovernmental treaty. Other policies have been implemented such as the strengthened Stability and Growth Pact, the Treaty on Stability, Coordination and Governance in the EMU (fiscal compact), the European Semester, the Euro Plus Pact and the new European system of financial supervision.

Any initiative to address other functions conducive to fiscal stability, economic growth, job creation and improved competitiveness would greatly increase the rationale for a specific euro area budget as it would provide a simple and transparent framework. A euro area budget with the above-mentioned functions would represent a shift from several intergovernmental agreements between Euro Area Member States and, if integrated into the EU framework, would fill the democratic accountability gap at least in part.

The detailed functions of a euro area budget, and the possible expenditure programmes linked to them, are not the subject of the present report and have been abundantly analysed elsewhere. However, a few analyses have given insights into their financing.

*The choice regarding how the euro area should be financed is not secondary and has an impact on its overall governance.*

The governance framework of a euro area budget would have an influence on its financing, and vice versa. In the course of history the financing of a political entity, or of an international organisation, has been instrumental in its development and its capacity to fulfil its tasks: this is therefore not a secondary aspect but a constitutional one. Whether such a budget should be sufficiently autonomous and have a reactive fiscal capacity will therefore have to be decided by the Member States, preferably from the beginning.

In this regard, the EU experience is contrasted: the Treaty of Rome envisaged first the financing of the Community budget via national contributions as a provisional mechanism, to be then replaced by own resources, but the evolution of the own resources system since 1988 has brought back as the main source of financing an own resource which is in fact perceived as a national contribution, as this report has explained at length (point 1.2.1). This in turn has fuelled the perception of the budget as a zero-sum game and prevented decisions being made on the basis of the general European interest. An efficient euro area budget should learn from this experience.

### *Possible sources of revenue for the euro area.*

Independently from these considerations, the possible sources of revenue to finance the euro area budget do not differ significantly from the possible candidates for own resources which have been examined for the future financing of the EU budget in Part 2. The Group considers, however, that the envisaged size of the euro area budget should be taken into account to devise the most suitable candidate or revenue mix. There is obviously no reason to conceive a complex mix of revenue if the size of the euro area budget is a fraction of the EU budget. Moreover, the size of a Euro area budget does not have to be fixed throughout time. It should be dependent on the economic momentum within the euro area and resources ought to be used to finance countercyclical measures.

As explained in the detailed analysis of the various candidates for EU own resources, some would appear more suitable in the euro area context because they are already linked to the existence of the Euro and the European system of central banks. This is the case of revenue from seigniorage, for instance, which amounts to approximately EUR 4-5 billion per year. This could be the case of revenue from the financial transaction tax (estimated at EUR 10-15 billion per year) if the enhanced cooperation currently under discussion comes to fruition and if concerned members wish to attribute such revenue to a visible European project. Should the euro area budget require higher amounts, revenue from a share of national indirect or direct taxation could be used or even cash contributions.

### *Collection of revenue*

As regards the collection of revenue for the euro area budget, it could be entrusted to Member States' administrations as is the case for the EU budget, if such revenue is based on existing national taxes. In the case of a completely new tax which is not currently collected at the national level, creating a collection administration at euro area level rather than in all euro area members could be a more efficient way to proceed and should be further explored. The Commission department in charge of the proper implementation of collection provisions for the EU budget would be entrusted with similar tasks in relation to the euro area budget, once these provisions have been agreed by the euro area budget authority. In this regard, the budget of the European Development Fund, which is not part of the EU general budget but is

managed entirely by the Commission, could provide a useful example.

### *Guiding principles for a euro area budget*

Finally, a euro area budget should be adopted according to the basic principles of public finance which generally apply to national budgets and the European budget alike, save some specific provisions required for the Euro Area:

- » unity: the euro area budget should show in a single document all revenue and all expenditure for the euro area;
- » universality or non-assignment: all revenue should finance all expenditure and not be specifically assigned. This principle is fully compatible with the setting of specific financing keys according to the various objectives/ functions, and ensures more flexibility in the implementation of the budget. In other words, equity/fairness is ensured ex-ante, when revenue — and the share of each Member States — are decided. A way to look at these functions is to assimilate them as three separate funds which would draw on a common source of funding with different arrangements for calling such resources;
- » accuracy: the euro area must not spend more than necessary, which means that revenue cannot be collected and expenditure cannot be affected unless it is booked to a budget line (and the necessary authorisation by the budgetary authority has therefore been given);
- » specification: the euro area budget needs to be detailed in a vertical and horizontal structure so that there is no ambiguity of purpose for all appropriations. Specification applies to both revenue and expenditure: the various sources of revenue must be clearly identified and the various types of expenditure must be clearly defined.

These principles aim at presenting a budgetary document which is at the same time simple, transparent and accountable.

Other principles which apply to the EU budget would not be necessarily relevant for the euro area and should be further examined:

- » annuality: if the euro area budget is annual, should it be framed in a multiannual perspective like the EU budget? This would seem relevant

only for the function of competitiveness, which would entail multiannual expenditure. The macroeconomic stabilisation and crisis management functions rather require as much flexibility as possible, and a strong reactive capacity to economic circumstances. This later aspect calls for an efficient governance structure.

- » equilibrium: if the creation of a euro area budget has a borrowing capacity, this principle should not apply for the euro area budget, at least not on an annual basis.

*RECOMMENDATION 9 – Allow for a certain degree of differentiation for the further development of the euro area.*

### **3.4. ‘Other Revenue’: possible sources of financing for the EU budget other than own resources**

Own resources are the major component of the EU budget revenue, but they are complemented by what is referred to in Article 311 of the TFEU as ‘other revenue’: ‘Without prejudice to other revenue, the EU budget shall be financed by own resources’.

The potential of other revenues has so far been neglected in the debate on EU financing. And the purpose here is not to present them as a credible alternative to own resources due to their high volatility and their total indifference to equity between Member States. The wording of the Treaty also implies that other revenue should remain marginal compared to own resources. Yet they are a component of EU budget income and their potential could certainly be explored further, in particular to address specific issues and make the EU budget more responsive.

*The choice regarding how the euro area should be financed is not secondary and has an impact on its overall governance.*

Indeed, these ‘other revenues’ have a more flexible legal character since they are not ruled and established through the ORD but rather in secondary law and thus would not require ratification by all Member States. Additionally, they could indeed represent a real ‘genuine’ income source for the EU budget by its link to EU policies and legal competences. The major weakness would be the unpredictable and unstable nature of such

revenues. For this reason they would be better used to feed a dedicated reserve rather than a policy requiring planning and stability in its financing.

All 'other revenues' are entered in the EU budget under one of the current different titles laid down on the revenue side, as shown in the excerpts from the draft budget for 2017 (Annex VIII). They allow for a wide range of income sources, from fines to surpluses or contributions from EU staff. In recent years, they were mainly composed of fines, while infringements and other sources were rather modest. In 2015, 'other revenue' represented 2.5% of the total EU budget revenue (excluding assigned revenue), while revenue under title 7 (interests on late payments, fines and penalties) represented around 50% of the total other revenue (EUR 1.7 billion).

Some items, such as the resulting surplus of the previous year (outturn) under Title 3, are governed by the own resources legislation, as it relates directly to the use of own resources. This is not always the case: revenue which is explicitly recorded as earmarked for a particular policy is meant to reinforce the corresponding budget lines on the expenditure side, and is therefore not counted against the ceilings of the multiannual financial framework. As a consequence, such revenue is not fungible with the residual GNI-based resource. As an example, EFTA or pre-accession countries wishing to partake in certain funding programmes can do so, on the basis of an agreement and a pre-defined contribution to the programme's financial envelope (e.g. Horizon 2020). Such contributions are recorded as 'external' assigned revenue.

However, there are several items under Title 7 of the EU budget which are considered as general revenue and which, once budgeted, result in a correspondingly lower need for the GNI-based own resources. The best known example is the fines stemming from competition and cartel cases. Once they are irrevocably applied, that is after all administrative and judicial remedies are exhausted, competition fines are entered as EU revenues via an amending budget, and are therefore accounted for against GNI contributions, which can lead to significant reductions to Member States' payments in some years.

Other examples are the excess emission premiums for new passenger cars, under Article 711 of the general budget of the EU. These are particularly interesting from the point of view of revenue in relation to the enforcement of an EU policy.

*'Other revenue' can be created through somewhat lighter procedures.*

Legally, such revenue sources are not established through the Own Resources Decision (ORD). They are anchored in secondary law and thus do not require ratification by all Member States like the ORD. For example, the Regulation setting emission performance standards for new passenger cars as part of the Union's integrated approach to reduce CO<sub>2</sub> emissions from light-duty vehicles (EC 443/2009) includes the following provision under Article 9(4): 'The amounts of the excess emission premiums shall be considered as revenue for the general budget of the EU'. In the annual budget, a token entry (p.m.) under Chapter 71 Fines, Article 711 lays down the structure for entering such premiums in the budget, should they materialise<sup>52</sup> (similar: EU 510/2011).

In a similar vein, the Treaty of Lisbon introduced new provisions which explicitly allow for the introduction of 'measures of fiscal nature' in the areas of energy and environment (Articles 192 and 194 TFEU). It is clear from these provisions that the fiscal aspect of such measures should remain secondary: their primary purpose is to contribute to achieving the objectives of the policy under which they are taken, such as promoting energy efficiency, renewables, the protection of the environment or the fight against climate change.

These provisions have not been used yet, but it could be envisaged that, once the primary justification has been established, the revenue stemming from such measures will enter the EU budget, either as general, 'other revenue', or earmarked to the same policy or purpose.

One case in point, although this was not the outcome decided at the time, concerns the proceeds of the auctioning of emission rights in the context of the European Emissions Trading System of greenhouse gases. These proceeds stem from EU level policy and legislation. Under present legal provisions, they are collected and retained by the Member States. Since the proceeds are sporadic and unpredictable they would not have constituted a very stable own resource. However, as an item of 'other revenue', the auctioning proceeds could have been a non-negligible component of EU budget income, and would have reduced the GNI contributions.

52. In the budget year 2015 there were around EUR 1.1 million in excess emission premiums.

It could also be argued that, if some revenues stem directly from a European policy, and would not exist otherwise, they should be entered in the budget. In a national context, the levying of fees, user charges, premiums, reimbursement of costs or auctioning proceeds are commonly considered as a useful and legitimate tool in policy making. This is not the case (yet) at the EU level, but it could be envisaged more systematically in the context of the preparation of the future generation of EU programmes, and this type of prospective income could be incorporated already at the stage of policy design.

It would probably not be the most appropriate to consider such income as an own resource, because it would have a distinct purpose in the concerned policy area and would not be established in the first place to finance the EU budget. In addition, by definition it would probably be very volatile and unstable, with sporadic or low proceeds. This is the case for competition fines: over the last 10 years, annual revenues have averaged roughly EUR 1.7 billion, with annual amounts varying between EUR 0.4 billion and EUR 4.2 billion.

*There is a strong case for 'other revenue' to finance the EU budget notably when they stem from policies linked to public goods or when national attribution would be controversial.*

However, like 'other' or 'miscellaneous' revenue, fines would follow the logic of a common policy decided upon at EU level and would have many advantages: they could enhance the efficiency and fairness of a policy, by enforcing common standards, including by means of fines or penalties for infringements (Example: the polluter-pays principle); they would also be transparent and visible to citizens who are used to this kind of tool at the national level. Moreover, in the well-established case of cross-border, single market-related competition fines, there is a high acceptance that this revenue should finance the EU budget: any other destination would certainly be much more controversial. It might be the case in the future that, for example as concerns the fight against pollution or climate change, the measures themselves and their economic incidence may encounter resistance, but the logic that these measures would benefit all EU citizens and participate to a European public good as such would give a strong argument to their being attributed to the EU level. Possible examples of 'other revenues' stemming from current of future

policy initiatives include revenues which will accrue from the EU system of border controls to enter the Schengen zone (ETIAS<sup>53</sup>), the European space strategy or the conservation of marine biological resources.

53. ETIAS: European Travel Information and Authorisation System.

## CONCLUSION

The deliberations of the High Level Group on Own Resources, and the discussions held during the Interinstitutional Conference with National Parliaments in September 2016, have made it clear that time is ripe for a comprehensive reform of the EU budget. Under the next financial framework period, the EU budget, its expenditure structure and its revenue side should and can be improved. While gradual improvements would also be possible over several MFFs, the Group considers that the conjunction between the emergence of new political priorities and the changes on the revenue side which will inevitably follow a departure of the UK from the EU presents a unique context which should be conducive to reform. Under such reform, the Union must mobilise common resources to find common solutions to common problems.

The Group reiterates what it has underlined throughout its mandate, i.e. that the changes it puts forward can be implemented under the current Treaty and, in general, under the current institutional set-up. The candidates for new own resources identified in the present report can be created while still respecting the fact that fiscal competences remain at the national level, and taking into account the overall constraint of budget neutrality so that the reform of own resources does not create additional tax burden on EU citizens. On the contrary, new own resources created in combination with a redirecting of expenditure on common public goods should lead to expenditure savings for Member States, if this is so wished.

In order to achieve the necessary decision-making requirements, and in particular the unanimity requirement in the Own Resources Decision and in the MFF, such a reform will have to satisfy a multitude of interests simultaneously. It could contain the following elements:

- » as regards the main expenditure items of the EU budget, they should be redirected towards the policies which produce the most European added value, or reformed in order to produce such added value. Policy areas like the better protection and management of the common external borders, defence and security as well as climate action and working towards a low-carbon economy are well beyond the inception stage. These are areas on which the legitimacy of EU action should be built within the next financial framework. Incidentally, they are also policy areas which in turn can justify new ways of

financing the budget, and sometimes create new revenue streams.

- » as regards revenue, the present report has highlighted the various merits and faults of about a dozen candidates for new own resources. Some already exist in the present system, work well and should be maintained, such as the traditional own resources and the GNI-based own resource as a residual source. Others can be further developed into many variants, depending on the criteria which would be given priority.

The Group has, in its evaluation of the various candidates, given particular attention to the four guidelines provided in the Group's mandate (simplicity, transparency, equity and democratic accountability). It has chosen, after careful consideration, to put forward candidates which can contribute to the provision of public goods and sustainability, and bring added value also on the revenue side, in order to align the funding of the EU with its long-term general objectives. Given the undisputed European dimension, the growth friendliness and the potential of double dividends, the cluster of taxes related to 'energy/environment/fight against climate change' features prominently on the list of potentially viable new own resources bases.

As a result, the new candidates identified can do more than merely ensuring sufficient financing for the EU budget. They can also, in some measure contribute more directly to policy objectives:

- » they can create incentives in the energy and environmental areas, for instance to fight climate change, by creating common taxes in Member States;
- » they can contribute to the achievement of the single market, by reducing free riders and tax competition when it is harmful, and by creating a level-playing field for economic actors;
- » they can reduce the red tape for economic actors, by encouraging the creation of a common tax instead of different national taxes targeting the same source, etc.

In addition, the Group has reflected on additional changes to the financing system of the EU which do not strictly concern own resources, but rather the architecture and the periphery of the system, some of which aim at optimising the links between the expenditure and the revenue sides:

- » a clear, shared terminology and presentation of how the EU is financed, both in the EU and national budgets, reflecting a common understanding of the legal, political and economic nature of own resources and other revenue;
- » thanks to the redirecting of EU expenditure towards policies with European added value, the abolishing of corrections on the revenue side, and the development of meaningful indicators to measure the costs and benefits of the EU for Member States and citizens;
- » the systematic exploration of new income sources which, if they are not suitable as new own resources, could nonetheless be allocated to the EU budget under the category of 'other revenue';
- » differentiated solutions if those are the only way forward to develop policies: enhanced cooperation and euro area-specific solutions, for example, should allow Member States that are willing to advance not to be blocked by those that may choose to join only at a later stage. The differentiation which has already been introduced under various forms in the treaties has consequences for the revenue side as well as the expenditure side, and any consideration for further differentiation should be carefully assessed and justified, in particular to determine the right balance between the aforementioned guidelines of the Group's mandate.

makers and budgetary actors to make some courageous choices and find the necessary momentum to adapt the EU budget to its time and challenges.

All the proposals summarised above are clearly set out in the recommendations of the Group, and should contribute to:

- » developing the leverage potential of the EU budget;
- » helping implement policies, supporting and accelerating the achievement of European objectives and the *acquis* across the Union, especially in cohesion countries;
- » attracting additional public and private co-financing through financial instruments;
- » incentivising structural reform and the translation of the country-specific recommendations into economic reality; and
- » finally, playing a modest but constructive role in a better overall fiscal coherence.

Building blocks have been presented; key notions and principles have been clarified. It is now up to the policy



## ANNEXES

<b>Annex I</b>	Joint Declaration on Own Resources (December 2013)
<b>Annex II</b>	The work of the Group
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## Annex I — Joint Declaration on Own Resources (December 2013)

1. According to Article 311 of the TFEU the Union shall provide itself with the means necessary to attain its objectives and carry through its policies; it also stipulates that, without prejudice to other revenue, the budget shall be financed wholly from own resources. Article 311(3) indicates that the Council, acting in accordance with a special legislative procedure, shall unanimously and after consulting the European Parliament adopt a decision on the system of own resources and that, in that context, the Council may establish new categories of own resources or abolish an existing category.
2. On this basis, the Commission presented in June 2011 a set of proposals to reform the Own Resources system of the Union. At its meeting of 7/8 February, the European Council agreed that Own Resources arrangements should be guided by the overall objectives of simplicity, transparency and equity. In addition, the European Council called on the Council to continue working on the proposal of the Commission for a new own resource based on value added tax (VAT). It also invited the Member States participating in the enhanced cooperation in the area of financial transaction tax (FTT) to examine whether it could become the base for a new own resource for the EU budget.
3. The question of own resources requires further work. To this end, a high-level Group will be convened, composed of members appointed by the three institutions. It will take into account all existing or forthcoming input which may be brought by the three European institutions and by National Parliaments. It should draw on appropriate expertise, including from national budgetary and fiscal authorities as well as independent experts.
4. The Group will undertake a general review of the Own Resources system guided by the overall objectives of simplicity, transparency, equity and democratic accountability. A first assessment will be available at the end of 2014. Progress of the work will be assessed at political level by regular meetings, at least once every six months.
5. National Parliaments will be invited to an inter-institutional conference during 2016 to assess the outcome of this work.
6. On the basis of the results of this work, the Commission will assess if new Own Resource initiatives are appropriate. This assessment will be done in parallel to the review referred to in Article 2 of the MFF Regulation with a view to possible reforms to be considered for the period covered by the next multiannual financial framework.

## Annex II — The work of the Group

### i. Establishment and composition of the High Level Group on Own Resources

The Group was established in April 2014 after the presidents of its three parent institutions jointly designated Mario Monti as its Chairman, and after each institution designated three members to contribute in a personal capacity to its work. The composition of the Group partially changed after the Juncker Commission took up its functions in November 2014.

Chairman (jointly appointed by the European Parliament, the Council and the Commission):

Mario Monti, member of the Italian Senate, President of Bocconi University, former Prime Minister of Italy and European Commissioner.

Members appointed by the European Parliament:

Ivailo Kalfin, former Member of the European Parliament, former Deputy Prime Minister of Bulgaria and Minister of Labour and Social Policy;

Alain Lamassoure, Member of the European Parliament (EPP Group), former Minister for European Affairs, then for Budget, of France;

Guy Verhofstadt, Member of the European Parliament (ALDE Group), former Prime Minister of Belgium.

Members appointed by the Council:

Daniel Dăianu, Member of the Board of the National Bank of Romania, former Member of the European Parliament and Finance Minister of Romania;

Clemens Fuest, President of the Ifo Institute for Economic Research, Munich, former President of the Centre for European Economic Research ZEW, Mannheim;

Ingrida Šimonytė, Deputy Chairwoman of the Board of the Bank of Lithuania, former Minister of Finance of Lithuania.

Members appointed by the Commission:

Kristalina Georgieva, Vice-President of the Commission in charge of budget and human resources, who replaced former Commissioners for financial programming and budget Janusz Lewandowski and Jacek Dominik;

Pierre Moscovici, Member of the Commission in charge of economic and financial affairs, taxation and customs, who replaced former Commissioner for taxation, customs, Algirdas Šemeta;

Frans Timmermans, First Vice-President of the Commission in charge of better regulation, inter-institutional relations, rule of law and Charter of fundamental rights, who replaced former Vice-President Maroš Šefčovič.

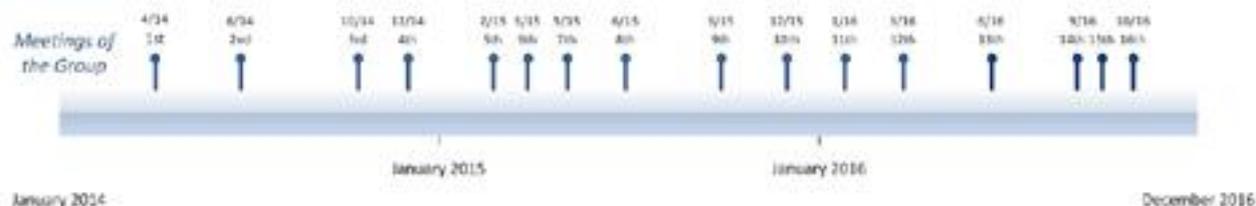
### ii. The Group's approach

The HLGOR built its strategy on the basis of all the aspects of its mandate, including its innovative inter-institutional format, its openness to academic research and existing literature on the issue, and its regular exchanges with the institutions in Brussels and with national parliaments, at their request. This novel way to proceed contrasted with past reports on own resources, which were more technical in nature and less immersed in the political environment. It also proved instrumental in setting the general tone of this report, which calls for a courageous, comprehensive and pragmatic approach which will require that all Member States refrain from a purely rhetorical stance and discuss some issues in substance before laying down too many red lines.

The Group has been asked to be bold and comprehensive in its appraisal of all the issues related to the system of own resources and therefore has not limited its discussions to the revenue side of the EU budget. In fact, the

pressing events and challenges which the EU had, and still has, to confront have made a complete reshuffle of spending priorities imperative. This fact, together with the sudden opportunity to unblock the rebates issue after more than 30 years, creates a unique backdrop for a root and branch reform of the EU budget.

The Group met [16] times – in bi-monthly meetings. Information about the meetings is available at: [http://ec.europa.eu/budget/mff/hlgor/events/meetings\\_en.cfm](http://ec.europa.eu/budget/mff/hlgor/events/meetings_en.cfm)



### iii. First assessment report

As foreseen in its mandate, the Group published its First Assessment report in December 2014. The document aimed at providing a solid and comprehensive analysis of the current system of own resources, of the recent negotiations and of the essential criteria and questions against which a future system should be evaluated. It was then subsequently presented to the presidents of political parties in the European Parliament at their meeting of 8 January 2015, to members of the Committee on Budget of the European Parliament at their meeting of 5 February 2015 and to EU ministers of finance at their meeting of 17 February 2015. The First Assessment report is available at: <http://ec.europa.eu/budget/mff/hlgor/library/reports-communication/FirstAssessmentReport-December2014.pdf>.

### iv. Hearings and contributions from external experts

Most Group meetings have given the opportunity to researchers, academics and practitioners to present and discuss selected areas of their expertise. Interestingly, most of them have in turn used this opportunity, or the First Assessment Report of the Group, to expand their analysis. As a consequence, the body of work publicly available on own resources has increased significantly over the last 2 years, providing updated analyses and sometimes figures on possible candidates. A more detail appraisal of these contributions is available at:

[http://ec.europa.eu/budget/mff/hlgor/events/index\\_en.cfm](http://ec.europa.eu/budget/mff/hlgor/events/index_en.cfm).

#### Contributions from external experts

- » Sustainability-oriented Future EU Funding by M. Schratzenstaller (WIFO), D. Nerudová (Mendel University Brno) — September 2016
- » Redesigning the Own Resources: Possible Contribution from the Banking Sector by V.Ceriani (Advisor for the MEF, Italy) — June 2016
- » Transferring Taxes to the Union The Case of European Road Transport Fuel Taxes by M. Thöne (FiFo) — March 2016
- » Keys for Contributions from the Banking Industry: Sharing the Burden of the Single Resolution Mechanism by A.Malchiodi (DG FISMA) — June 2016
- » Sustainability-oriented Future EU Funding by M. Schratzenstaller (WIFO)& D. Nerudová (Mendel University Brno) —xxx

- » Digital Sector Based Own Resource by G. Papa (DG CONNECT) — September 2015
- » Transport charges and taxes by R. Diemer (DG MOVE) — September 2015
- » How is the budget financed and why we need to change it? by A. Montagnon (DG BUDG) — September 2015
- » An own resource based on VAT by S. Lehner (DG Budget) — March 2015
- » Reforming 'Own Resources', reforming the EU Budget? by G. Cipriani (ECA) — February 2015
- » Governance of the EU: Implications for and of OR by I. Begg (EUI, LSE) — October 2014
- » Research in economics (and political science) on reforming the EU OR System by C. Fuest (Ifo) — June 2014

## v. External study

As underlined in the First Assessment Report of the Group, there is already a substantial amount of technical analyses and data on the current system of own resources and on possible avenues for reform, stemming from academia or from proposals previously supported by the various institutional actors in past negotiations. However, what is missing is a comprehensive appraisal of the broader context in which the financing system of the EU budget is negotiated and decided as well as the 'success parameters' of the decision making process. The Group therefore commissioned a consortium of researchers led by the Centre for European Political Studies (CEPS)<sup>1</sup> to produce a study to draw lessons from the experience with previous negotiations. The study was published in June 2016 and is publicly available. It places the EU budget in the context of the many challenges that the EU faces today and, as a result of intense exchanges with the HLGOR, its findings are largely reflected in the present report. The study is available at:

[http://ec.europa.eu/budget/mff/hlgor/library/highlights/hlgor-studies-external-studyonfinancingofeu-budget-june-2016\\_en.pdf](http://ec.europa.eu/budget/mff/hlgor/library/highlights/hlgor-studies-external-studyonfinancingofeu-budget-june-2016_en.pdf).

## vi. Conference with National Parliaments

As foreseen in the mandate of the Group, an inter-institutional conference with National Parliaments was organised to hear the views of national parliamentarians in particular on key issues identified by the Group. The Conference took place on 7/8 September 2016 in the premises of the European Parliament in Brussels and brought together parliamentarians from almost all Member States, representatives of the European Institutions and members of the High Level Group on Own Resources .

Information on the conference is available at:

[http://ec.europa.eu/budget/mff/hlgor/conference/index\\_en.cfm](http://ec.europa.eu/budget/mff/hlgor/conference/index_en.cfm)

## vii. Regular reporting to political decision-makers

In what is an original feature of the way the Group's working method, regular reporting was made to the European Parliament, the Council and the Commission in various settings. This has allowed the analysis to mature and to take into account the significant changes in the political and geostrategic backdrop that may influence the future

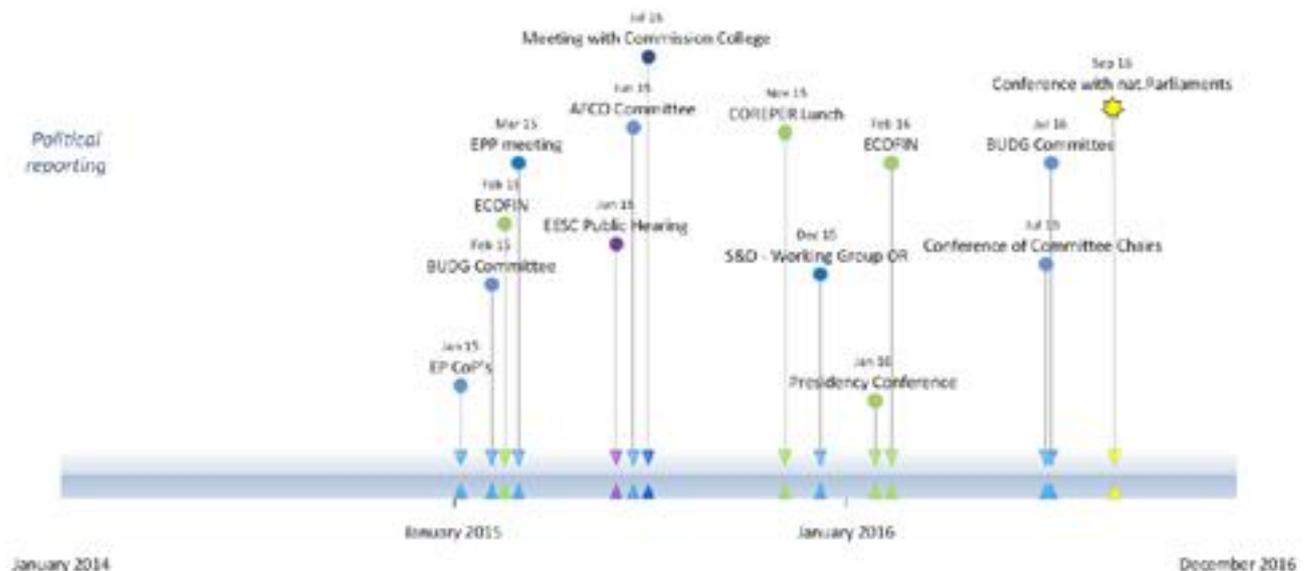
1. Study on the potential and limitations of reforming the financing of the EU budget, 3 June 2016, CEPS, Université de Pau et des Pays de l'Adour, LSE Enterprise and Deloitte (Jorge Núñez Ferrer, Jacques Le Cacheux, Giacomo Benedetto and Mathieu Saunier).

2. Documents relating to the Conference and press articles are available on the HLGOR website: [http://ec.europa.eu/budget/mff/hlgor/index\\_en.cfm](http://ec.europa.eu/budget/mff/hlgor/index_en.cfm)

financing of the EU, in particular the new or persistent crises the EU faces: the migration crisis, the internal and external security crisis, the environmental crisis, and the consequences of the financial and economic crisis of 2008 which have all contributed to a redefinition of EU priorities. In the last months of the Group's work, the result of the referendum on the United Kingdom's withdrawal from the European Union has given an entirely new twist to the prospect of reforming the EU budget on the revenue side, as one of the strongest locks on past negotiations will be lifted, namely the UK rebate. As the UK rebate had a quasi-constitutional protection, it gave the UK a very advantageous negotiating position on matters related to the own resources system, in particular compared to other net contributors. This will no longer be the case and for the first time, the own resources system can be revisited from a clean slate.

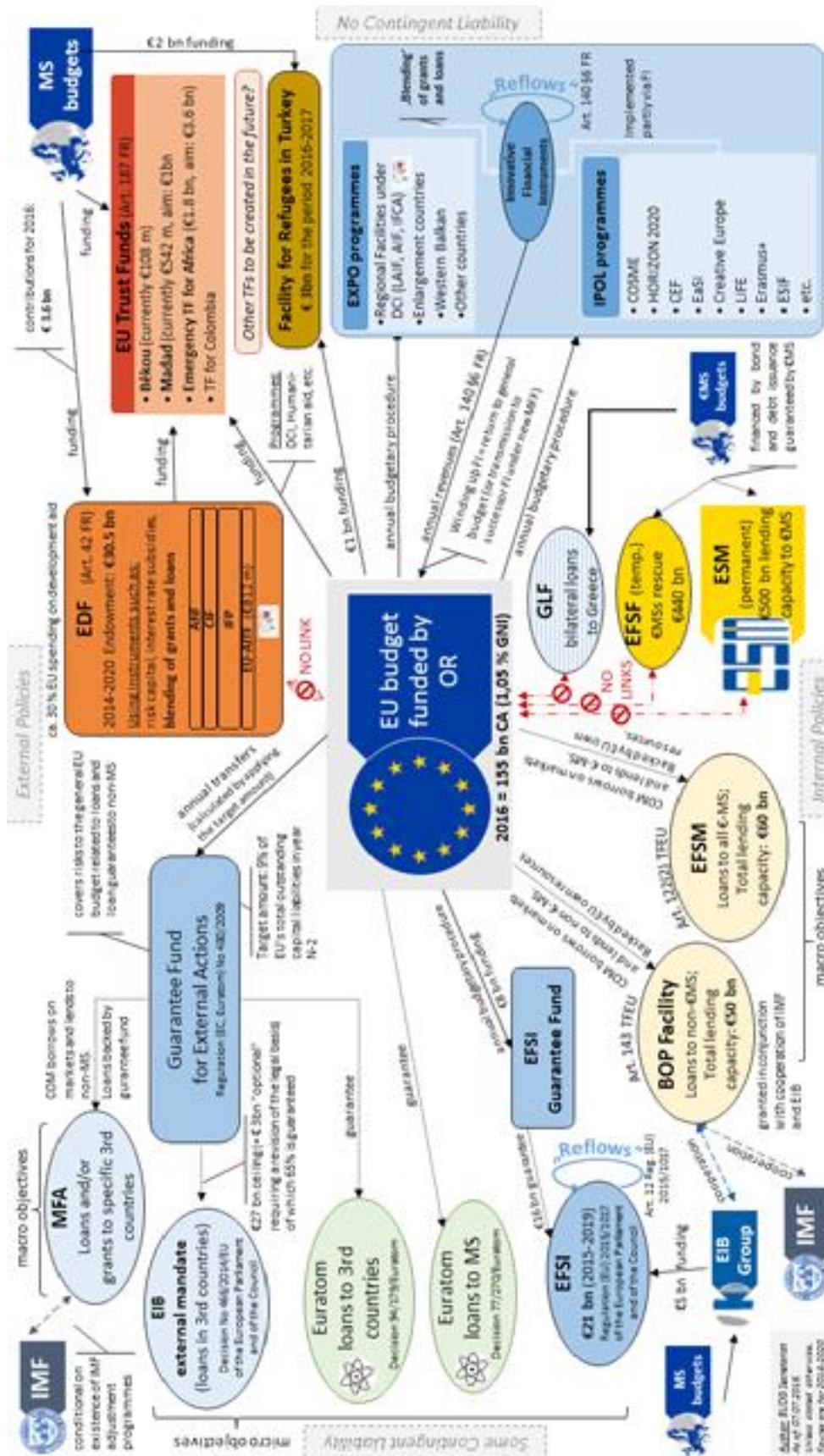
How these opportunities will translate into the future EU budget will depend, in part at least, on the shared awareness that both the structure of expenditure and their financing need reform (detailed reporting per institution is presented in Annex IV).

## Annex III — Detailed reporting of the work of the HLGOR per institution: dates, configuration



- » European Parliament: Brussels, 8 January 2015 Conference of the Presidents  
Presentation of the 'First Assessment' report
- » European Parliament: Brussels, 5 February 2015, Committee on Budgets  
Presentation and discussion of the 'First Assessment' report
- » European Parliament: Brussels, 2 March 2015 — Meeting with the EPP group  
Discussion with party representatives
- » European Parliament: Brussels, 17 June 2015, AFCD Committee  
Exchange of views with A. Lamassoure and G. Verhofstadt
- » European Parliament: Brussels, 8 December 2015, S&D Horizontal Working Group OR  
Discussion with party representatives
- » European Parliament: Strasbourg, 5 July 2016, Committee Chairs  
Discussion with VP K. Georgieva
- » European Parliament: Brussels, 12 July 2016, Committee on Budgets  
Exchange of views with Mario Monti
- » Inter-institutional conference with National Parliaments: Brussels, 7 and 8 September 2016  
Information on the conference is available at:  
[http://ec.europa.eu/budget/mff/hlgor/conference/index\\_en.cfm](http://ec.europa.eu/budget/mff/hlgor/conference/index_en.cfm)
- » Council: Brussels, 5 November 2014, COREPER II Lunch  
Discussion with Mario Monti
- » Council: Brussels, 17 February 2015, Economic and Financial Affairs Council (Ecofin)  
Presentation of the 'First Assessment' report
- » Presidency Conference: Amsterdam, 28 January 2016  
Exchange of views on future prospects for EU financing with VP Georgieva and Mario Monti
- » Council: Brussels, 12 February 2016, Economic and Financial Affairs Council (Ecofin)  
State of play of the HLGOR work
- » European Commission: Brussels, 1 July 2015, meeting with Commission College  
Presentation of the state of play of the HLGOR work and exchange of views
- » European Economic and Social Committee (EESC): Brussels, 1 June 2015, Public hearing  
Public hearing and exchange of views with and Commissioner with Mario Monti

Annex IV – The galaxy around the EU budget – an illustration of the complexity of the financing of EU activities



Source: illustration prepared for the Committee on Budgets of the European Parliament, updated on 1.7.2016. Figures for 2014-2020 unless stated otherwise. Disclaimer: As an illustration this chart is only one of several possible representations and may not be complete.

## Symbols and Abbreviations

- Flows of funding  
 -----→ Guarantees  
 ←-----→ Cooperation  
 ←- - - - -⊘- - - - -→ No link to the EU budget

AfF	Africa Investment Facility	EU-AITF	EU-Africa Infrastructure Trust Fund
AIF	Asia Investment Facility	Euratom	European Atomic Energy Community
Art.	Article	EXPO	External policies
bn	Billion	FI	Financial instruments
BOP	Balance-of-Payments Facility	FR	Financial Regulation
CA	Commitment appropriations	GNI	Gross National Income
CEF	Connecting Europe Facility	GLF	Greece Loan Facility
CIF	Caribbean Investment Facility	IFCA	Investment Facility for Central Asia
COSME	EU Programme for Competitiveness of Enterprises and Small and Medium-sized Enterprises	IFP	Invest Facility for the Pacific
DCI	Development Cooperation Instrument	IMF	International Monetary Fund
EaSI	EU Programme for Employment and Social Innovation	IPOL	Internal policies
EDF	European Development Fund	LAIF	Latin America Investment Facility
EFSF	European Financial Stability Facility	LIFE	L'Instrument Financier pour l'Environnement [Financial Instrument for Environment]
EFSI	European Fund for Strategic Investments	m	Million
EFSM	European Financial Stabilisation Mechanism	MFA	Macro-financial assistance
EIB	European Investment Bank	MS	Member States
ESIF	European Structural and Investment Funds	OR	Own Resources
ESM	European Stability Mechanism	TF	Trust Funds
EU	European Union	TFEU	Treaty on the Functioning of the European Union

## Explanations

### Guarantee Fund for External Actions (Council Regulation (EC, Euratom) No 480/2009)

<http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=URISERV%3A134006>

As a result of its loans to third countries and guarantees covering loans to finance investment operations in these countries, the European Union is exposed to financial risks. It was with the aim of protecting against such risks that the EU adopted the Regulation establishing a Guarantee Fund for external actions.

The target amount refers to the amount of resources required by the Fund in order to fulfil its mission. The Fund's target amount is set at 9% of the EU's total outstanding capital liabilities arising from each loan or guarantee operation, increased by unpaid interest due. The difference between the target amount and the actual value of the Fund's assets is paid from the general budget of the EU into the Fund, or to the budget in the event of a resulting surplus in the Fund.

The provisioning amount is calculated at the beginning of financial year 'n' on the basis of loans granted and guaranteed during the previous financial year ('n-1'). The amount thus calculated is entered in the budget of year 'n+1'. There is therefore a delay of approximately 2 years between the time when the amounts become outstanding and the actual provisioning of the Fund.

## **Innovative Financial Instruments in EU external policies (blending)**

[http://ec.europa.eu/europeaid/policies/innovative-financial-instruments-blending\\_en](http://ec.europa.eu/europeaid/policies/innovative-financial-instruments-blending_en)

Blending is an instrument for achieving EU external policy objectives, complementary to other forms of providing aid and pursuing the relevant regional, national and overarching policy priorities. The principle of the mechanism is to combine EU grants with loans or equity from public and private financiers.

The EU grant element can be used in a strategic way to attract additional financing for major investments in EU partner countries by reducing exposure to risk. On a case-by-case basis, the EU grant contribution can take different forms to support investment projects:

- » investment grant & interest rate subsidy — reducing the initial investment and overall project cost for the partner country;
- » technical assistance — ensuring the quality, efficiency and sustainability of the project;
- » risk capital (i.e. equity & quasi-equity) — attracting additional financing;
- » guarantees — unlocking financing for development by reducing risk.

## **EU Trust Funds for External Actions**

[http://www.europarl.europa.eu/RegData/etudes/BRIE/2015/572797/EPRS\\_BRI\(2015\)572797\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2015/572797/EPRS_BRI(2015)572797_EN.pdf)

Since January 2013, the new Financial Regulation applicable to the EU budget allows the European Commission to create and administer Union trust funds in the field of external action: these are multi-donor trust funds for emergency, post-emergency or thematic actions. The European Parliament welcomed this development in an April 2013 resolution, considering that it would allow the EU to raise the visibility of its external action and to have greater control over the delivery chain of relevant funds. The first two EU trust funds were created in 2014: the Bêkou EU Trust Fund (EUR 108 million), focusing on the stabilisation and reconstruction of the Central African Republic and the Madad Fund (EUR 542 million), dealing with the response to the Syrian crisis. As part of intensifying efforts to tackle the refugee crisis, the European Commission and Spain have also set up an Emergency Trust Fund for stability, to address the root causes of irregular migration and displaced persons in Africa. The new fund has an initial budget of EUR 1.8 billion and targets 23 countries in the Sahel and the Lake Chad region, the Horn of Africa and North Africa. The bulk of funding has so far come from the EU budget and the European Development Fund (EDF). By comparison, Member State contributions to the trust funds have to date been relatively low. The European Commission and the European Parliament are therefore urging Member States to match the EU budget and EDF contributions to the trust funds. The Commission's aim is to increase the amounts in the Madad Fund and the Emergency Trust Fund for Africa to EUR 1 billion and EUR 3.6 billion respectively.

## **Balance-of-Payments Facility**

<https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-387-EN-F1-1.PDF>

Balance-of-payments (BOP) assistance under Article 143 of the Treaty on the Functioning of the European Union (TFEU) and Council Regulation (EC) No 332/2002 of 18 February 2002 establishing a facility providing medium-term financial assistance for Member States' balances-of-payments (BOP Regulation) takes the form of medium-term loans provided by the Union.

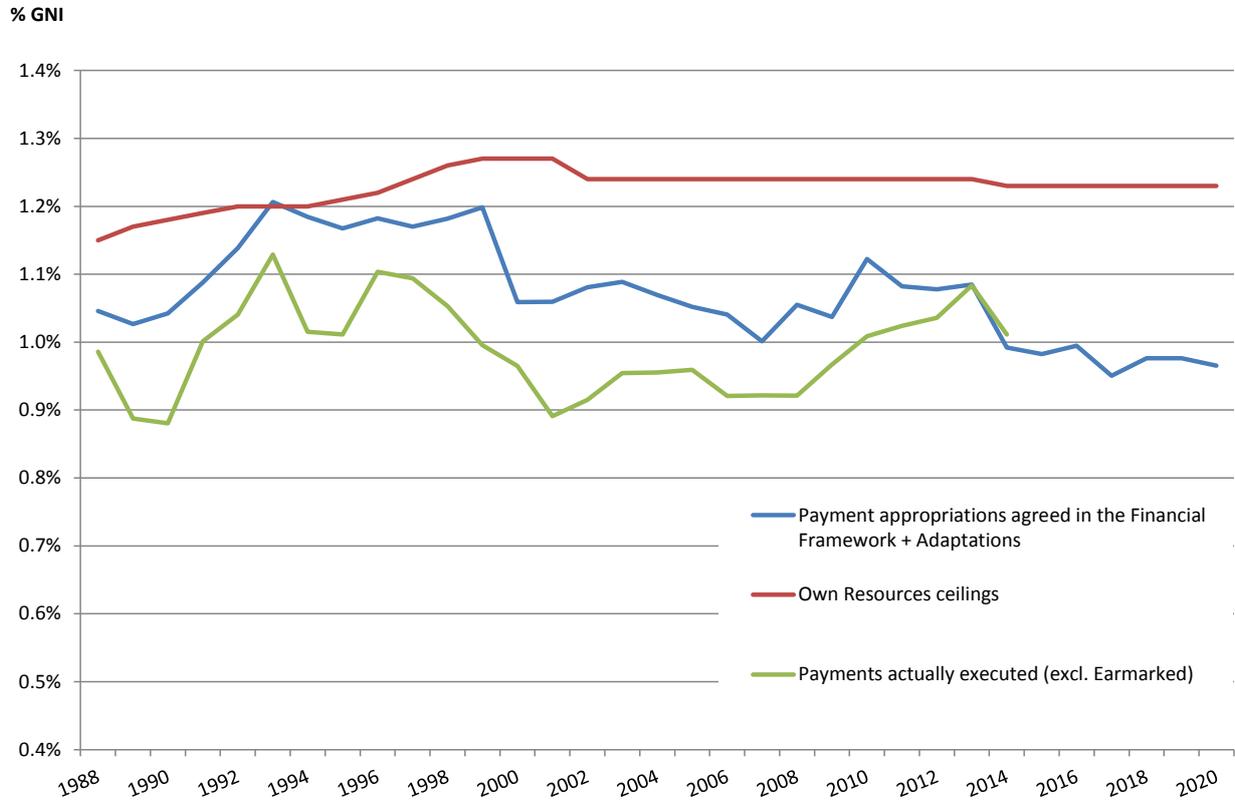
It is generally granted in conjunction with financing by the International Monetary Fund (IMF) and other multilateral lenders, such as the European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD) or the World Bank.

## **European Financial Stabilisation Mechanism (Council Regulation (EU) No 407/2010)**

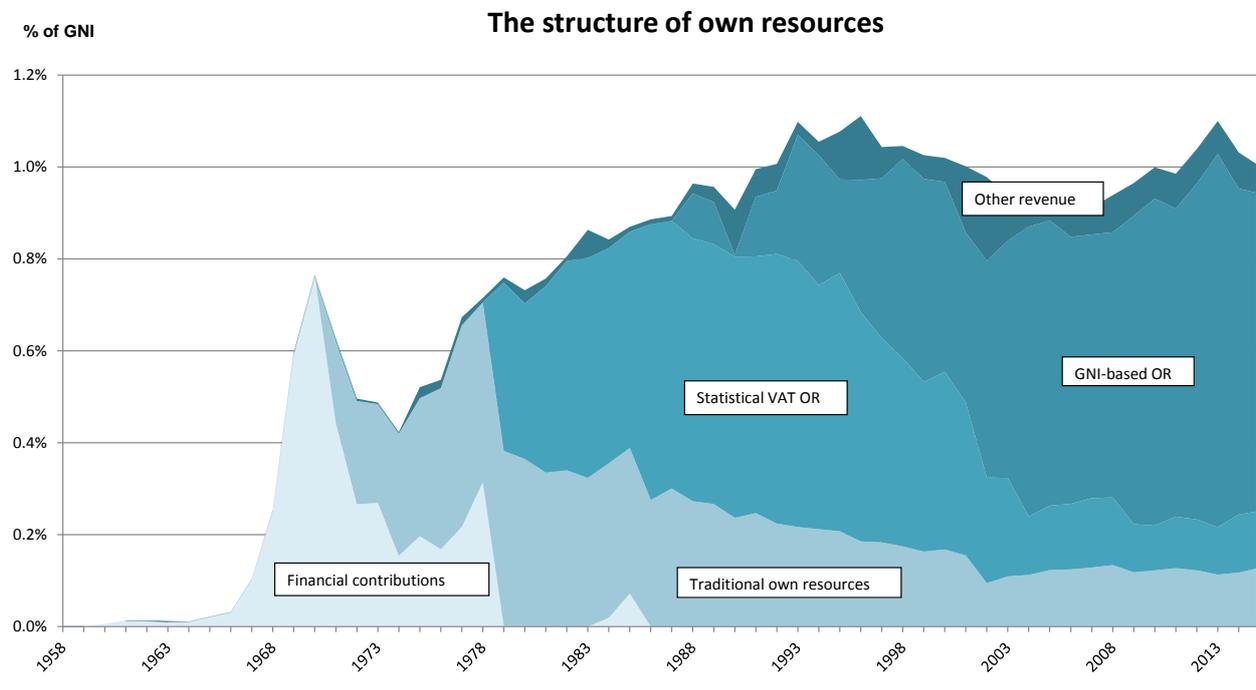
<https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-387-EN-F1-1.PDF>

Council Regulation (EU) No 407/2010 of 11 May 2010 established the European Financial Stabilisation Mechanism (EFSM) based on Article 122(2) TFEU. The EFSM is fully backed by the EU budget and has a total lending capacity of up to EUR 60 billion.

Annex V — Changes of the own resources ceiling, the MFF ceiling and the payments executed since 1988



## Annex VI — The structure of own resources



Source: elaboration, European Commission

Annex VII — Evaluation and ranking of the own resources examined by the HLGOR

Current own resources which the Group considers should be maintained								
	1	2	3	4	5	6	7	8
GNI-based OR								
Traditional Own Resources (TOR)								
Current EU VAT								
Options for new own resources								
	1	2	3	4	5	6	7	8
CO2 levy / Carbon pricing								
Inclusion of the EU Emission Trading Scheme proceeds								
Motor fuel levy								
Electricity Tax based OR								
CCCTB, EU corporate income tax								
FTT								
Bank levy								
EU VAT reformed								
Seigniorage								



- Criteria:
1. Equity/Fairness
  2. Efficiency
  3. Sufficiency & Stability
  4. Transparency & Simplicity
  5. Democratic accountability & budgetary discipline
  6. Focus on European added value & constrain narrow self-interest
  7. Subsidiarity principle
  8. Limit political transactions costs

## GNI-based OR

<b>1. Equity/Fairness</b>	Perceived as equitable and fair among MS (as % of GNI): it respects the ability to pay of MS, even if nuanced by corrections. Equity at the level of citizens (as GNI per head) is not straightforward: the redistributive effect between MS and between taxpayers is therefore less clear and, in any case, only indirect.	
<b>2. Efficiency</b>	The current system of the GNI contributions has proved very efficient. The calculation of the contributions is a clear and fair process.	
<b>3. Sufficiency &amp; Stability</b>	The GNI-based OR is instrumental in providing stability and sufficiency to the revenue of the EU budget, both annually and in the medium term.	
<b>4. Transparency &amp; Simplicity</b>	GNI-based contributions are in theory simple, based on the share of each MS in the total EU GNI; however, corrections and different treatment in national budgets might hinder transparency.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	The GNI contributions are transferred automatically, in accordance with the ORD; the underlying GNI statistics are the result of a well-framed statistical exercise. However, how these 'national contributions' are presented in national budget contributed to create political pressure.	
<b>6. Focus on European added value</b>	There is no link between the GNI-based own resource and EU policies; although these contributions are the focus of national interests in multiannual budgetary negotiations.	
<b>7. Subsidiarity principle</b>	The GNI-based OR is not a tax and does not impact the fiscal preferences of MS. Well balanced responsibilities: the same GNI calculation rules apply to each MS, the underlying data are produced nationally and commonly agreed at European level.	
<b>8. Limit political transactions costs</b>	Increased political transaction costs: the GNI-based OR can be strongly influenced by political, economic and financial factors internal to each MS, and can create constraints to the negotiations of the EU budget when it is mostly seen as a national contribution.	

## Traditional Own Resources (TOR)

<b>1. Equity/Fairness</b>	TOR area "genuine" resource, since directly linked to a central EU policy –the Single market. TOR have an equal impact on taxpayers across the EU (horizontal equity), and most TOR are normally collected from the focal points of EU trade. However, the collection costs remain a sensitive issue, since they might be considered as a 'hidden' rebate.	
<b>2. Efficiency</b>	The current system has proved efficient and has not raised major concerns in its implementation.	
<b>3. Sufficiency &amp; Stability</b>	The share of TOR has steadily decreased over the years, and now it has stabilised around 12% of the EU budget. It therefore remains a non-negligible source of revenue for the EU budget.	
<b>4. Transparency &amp; Simplicity</b>	Being the only fiscal resource fully transferred to the EU level, TOR appear as a transparent and simple resource.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	TOR do not particularly score individually on this criteria.	
<b>6. Focus on European added value</b>	There is no link between TOR and EU policies.	
<b>7. Subsidiarity principle</b>	TOR are the only tax directly stemming from the existence of the Single Market, thus its proceeds are logically transferred and supervised at the EU level. The transfer of fiscal power is enshrined in the Treaty.	
<b>8. Limit political transactions costs</b>	The collection of TOR at national level allowed pre-existing national customs authorities to continue to perform most of their tasks, and minimal central services at the EU level perform controls and oversight. Overall the implementation of the TOR rules seems satisfactory to MS.	

## Current EU VAT

<b>1. Equity/Fairness</b>	Equity is ensured by the reduction of the call rate of the VAT-based own resource for a group of MS, in order to balance its regressive nature. However, this provision aims at equity and fairness between MS, not between EU taxpayers.	
<b>2. Efficiency</b>	The current system is simpler, more transparent and more efficient than the previous complex 'frozen' rate system. Nevertheless, calculation remains cumbersome regarding the establishment of the theoretical VAT base built on highly complex statistical sets of data which vary in each MS.	
<b>3. Sufficiency &amp; Stability</b>	The share of the revenue accruing from the VAT-based own resource would be fixed by the call rate or the fixed rate applied to the VAT base. The VAT-based own resource is considered a reliable source of revenue with limited volatility.	
<b>4. Transparency &amp; Simplicity</b>	The current calculation of the theoretical VAT-base can raise transparency questions as it is complex, statistically-based and far from the real VAT collected revenue.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	The VAT-based OR as part of the overall financing system of the EU budget is approved by the MS in accordance with their respective constitutional requirements, is subject to EP scrutiny, to the Court of Auditors audits and to COMM services control. Nat. Parliaments are only involved in the real VAT collected revenue for the national budgets.	
<b>6. Focus on European added value</b>	The current VAT-based OR is calculated in accordance with the provisions of a common EU directive, although it remains a statistical construct. VAT could also play a part of a wider effort on VAT fight against fraud and VAT tax harmonisation in the EU.	
<b>7. Subsidiarity principle</b>	Current system has high administrative costs, which are, however, already foreseen and implemented both at national and European level.	
<b>8. Limit political transactions costs</b>	Since VAT is collected within a well-established EU harmonised legal basis, political transaction costs can be considered to be low. The European Council (Feb.2013) already expressed its support to the revision of VAT based OR, and this shows interest for a future OR based on VAT.	

## CO2 levy / Carbon pricing

<b>1. Equity/Fairness</b>	As a OR, a carbon tax-based could be questioned by MS, given that the CO2 intensity of the economy differs significantly across MS. Distributional impacts have to be addressed for improving fairness and ability to pay. A basket of OR could help neutralize asymmetrical effects or other types of 'compensations' could be agreed.	
<b>2. Efficiency</b>	An EU-wide CO2 gives economic actors more legal certainty and reduce compliance costs; it also serves EU environmental-friendly objectives and address the problem of users not facing the full (social and environmental) costs of their actions. Depending on its design, it could also play an important role on the elimination of the discrimination between EU producers on the internal and world markets.	
<b>3. Sufficiency &amp; Stability</b>	The potential tax base is sizeable enough to cover a large part of the EU budget. A carbon tax should primarily aim at changing energy consumption behaviour for reducing within the larger perspective of moving toward a low-carbon economy. Stability is a secondary objective.	
<b>4. Transparency &amp; Simplicity</b>	A EU-wide CO2 tax would bring more transparency and harmonisation to taxes between MS; it would also play a role in the avoidance of double taxation. As for the EU budget, transparency and simplicity would depend on the implementation and making available rules of a carbon tax as an OR.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	A carbon taxation would reduce GNI-based contributions and therefore respect the budgetary disciplin. It could significantly improve democratic accountability if the link with the objective of environment protection is clearly made both at EU and MS' level.	
<b>6. Focus on European added value</b>	A common, coherent carbon pricing policy including a CO2-taxation at EU level would be more effective than national approaches, in terms of environmental integrity, economic efficiency as well as political impact. Studies have shown that a carbon / CO2 tax could also contribute to economic growth.	
<b>7. Subsidiarity principle</b>	The carbon tax would be introduced by a directive and it would include min. levels of taxation; MS have to implement the directive and introduce/adjust national legislation; actual levying of the tax would take place at MS level. The OR decision (including ratification requirement) would provide the revenue sharing arrangement and the principle of transfer of such tax to the EU budget.	
<b>8. Limit political transactions costs</b>	The introduction of a Carbon / CO2 tax is very likely to encounter a strong hostility by the transports and fuel industries. It should also be envisaged as part of a more comprehensive package in order to accommodate Member States more dependent on carbon based fuels so that the fairness of the system is ensured.	

## Inclusion of the EU Emission Trading Scheme proceeds

<b>1. Equity/Fairness</b>	Phase 3 of the ETS (2013-2020) has brought significant harmonisation of the system at European level. However, it does not directly change the underlying differences between the energy sector and the economic structure of MS.	
<b>2. Efficiency</b>	There is no differentiation between MS, which therefore creates a common basis for an EU OR.	
<b>3. Sufficiency &amp; Stability</b>	Data are scarce and the demand has been consistently low so that price levels and auctioning proceeds have in any case been significantly below the tentative estimations. Potentially low or volatile income must be factored in.	
<b>4. Transparency &amp; Simplicity</b>	Collection and administration of current ETS revenue is ensured at the national level; collecting it as an OR would simply entail a simple transfer of part or all of this revenue to the EU level.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	ETS revenue would reduce GNI-based contributions and therefore respect the budgetary disciplin. It could significantly improve democratic accountability if the link with the objective of environment protection is clearly made both at EU and MS' level.	
<b>6. Focus on European added value</b>	ETS have a strong relation to European added value due to its direct link to the single market and to the objectives of EU environmental policy.	
<b>7. Subsidiarity principle</b>	ETS strongly focusses on cross-border activities and their impact in terms of emissions, it has increasingly harmonised rules (phase 3) contributing to creating a level-playing field within the single market and is established at the appropriate governance level for subsidiarity. Attribution of its proceeds as an OR would be decided by MS.	
<b>8. Limit political transactions costs</b>	Political transaction costs would be limited as the essential tools for enforcing the collection of such revenue are already into place. However, since it is currently revenue for national budgets it would certainly encounter strong resistance.	

## Motor fuel levy

<b>1. Equity/Fairness</b>	A motor fuel tax would respect the principle of "user-payer" or "polluter pays", if applied as well to sectors/industries which currently benefit from significant exemptions. However, as existing national taxes constitute a significant share of national budgets and have different weights throughout MS, it can be expected that finding the right and equitable balance will require some forms of compensations or progressiveness.	
<b>2. Efficiency</b>	A common taxation scheme would improve overall efficiency and reduce market distortion (tank tourism). In terms of collection, it would be very efficient since it would rely on existing mechanisms. Such taxes are already collected by national authorities.	
<b>3. Sufficiency &amp; Stability</b>	The motor fuel tax has a very significant revenue potential and could cover all or a very large share of EU budget needs, depending on its design (full or partial transfer). The consumption levels of motor fuel are rather stable; however, since it is geared towards environment protection, consumers would tend to change their behaviour.	
<b>4. Transparency &amp; Simplicity</b>	A motor fuel tax OR is simple and transparent for the tax payer, in particular if the percentage/amount attributed to the EU budget is shown on the receipt and if the base for this tax is fully harmonised and the collection centralised. However, it would only show the 'costs' of the EU, while the benefits would remain hidden.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	In case of a complete shift to EU-level, democratic accountability and budgetary discipline would need to be ensured through an enhanced role and responsibility of the EP. It would decrease the GNI-based own resource and therefore ensure budgetary discipline.	
<b>6. Focus on European added value</b>	A motor fuel own resource would reinforce the credibility and efficiency of the action of both-based the EU and its MS against climate change. A common and harmonised motor fuel tax would have more impact than national taxes in terms of environmental integrity, economic efficiency as well as political signal to the international community.	
<b>7. Subsidiarity principle</b>	The collection of such tax would still be ensured by Member States' collection authorities.	
<b>8. Limit political transactions costs</b>	A motor fuel tax could encounter significant opposition from MS who use such tax as an important and flexible fiscal tool, or by regions or industries that benefit from reduced rates or even exemptions.	

## Electricity Tax based OR

<b>1. Equity/Fairness</b>	An electricity tax on consumption would respect equity and fairness at macroeconomic level, since linked to income. Although, corrections or compensations to poorer households. Harmonisation efforts would be very high for countries where such taxation is very low.	
<b>2. Efficiency</b>	Current taxes on electricity are already efficiently collected by national authorities, via distribution companies. Moreover, because electricity is a basic consumption good and cannot be 'replaced'.	
<b>3. Sufficiency &amp; Stability</b>	The introduction of an electricity tax as an own resource could provide for a very large share of revenue depending on the share or percentage applied. Volatility is low.	
<b>4. Transparency &amp; Simplicity</b>	The collection of an electricity tax is simple, in particular if applied as a share or percentage of the total tax on the electricity bill. Complexity could come on how the electricity tax is used as a policy tool (social policy e.g.) and the related tax reductions and exemptions.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	No particular role on enhanced accountability or budgetary discipline.	
<b>6. Focus on European added value</b>	There is a clear link with the EU internal market and it could also play a role in relation with the EU environmental and energy saving policies. However, for electricity price reduction to EU citizens, it should be implemented as a shift from national tax revenues to EU revenue.	
<b>7. Subsidiarity principle</b>	As the collection of such tax already exists in Member States, the European tax could also be collected at the national level and a new OR decision, after adoption and ratification by all MS, would provide the revenue arrangements and the principle of transfer to the EU budget.	
<b>8. Limit political transactions costs</b>	Political costs would be high for a number of MS because current EU legislation sets very low minimum levels of taxation and there are big differences between tax rates of MS.	

## CCCTB, EU corporate income tax

<b>1. Equity/Fairness</b>	CCCTB is instrumental to make the single market more competitive and fairer, by ensuring that every company, no matter its size, pays its taxes where it makes its profits. It is strongly linked to the fight against tax avoidance.	
<b>2. Efficiency</b>	One of the main objectives of CCCTB is to create a simpler and more business-friendly tax environment in the EU.	
<b>3. Sufficiency &amp; Stability</b>	Depending on the rate applicable to the CCCTB once this is established and consolidated, it could represent a substantial share of EU financing, but there are important differences in MS.	
<b>4. Transparency &amp; Simplicity</b>	Transparency is the foundation of the CCCTB, because it entails MS automatic exchange of information. At the stage of the consolidated base it could allow businesses to fill only one set of tax papers for their entire EU operations, enhancing a level-playing field, legal certainty and reducing obstacles when operating cross-border.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	By contrasting hidden preferential regimes and harmful tax rulings, CCCTB is a tool to restore confidence in national tax systems and allows MS to re-focus their resources on growth-friendly taxation and to support wider socio-economic needs.	
<b>6. Focus on European added value</b>	The European added value in fiscal matters is at its highest in the case of the CCCTB, given its close link to deepening the single market and making it fairer.	
<b>7. Subsidiarity principle</b>	A corporate tax will require changes in national fiscal policies but a harmonised tax base at EU level appears to be a means for MS to regain fiscal sovereignty. In this sense, it is in line with the subsidiarity principle as only at the EU level such negative externalities can be tackled.	
<b>8. Limit political transactions costs</b>	Given the very diverse fiscal landscape concerning corporate taxes, and the positioning of a small number of countries at the head of tax competition in this area, political agreement will be difficult; although the numerous recent tax scandals have increased the pressure to act in many MS.	

## FTT

<b>1. Equity/Fairness</b>	An FTT would have positive equity effects between economic actors, partially compensating for the tax advantages to the fin. sector (VAT exemption and state aid). As for horizontal equity however, FTT is perceived by some as unfair for the concentration of fin. transactions and fin. institutions in few countries.	
<b>2. Efficiency</b>	The introduction of a common system for the FTT would reduce the current possibilities of tax avoidance, would ensure a more coherent tax framework and eliminate a source of fragmentation of the current Internal Market within the FTT jurisdiction.	
<b>3. Sufficiency &amp; Stability</b>	The high volatility of financial transactions could generate unpredictability of revenue. The volume of expected revenue from FTT, it would depend on the final design of the tax itself.	
<b>4. Transparency &amp; Simplicity</b>	The FTT aims at using a single harmonised tax, which will provide for the companies submitted to it a simpler tax framework than different national ones.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	FTT proceeds would accrue to the EU budget and reduce the GNI-based contributions, thereby having no impact on the volume of the EU budget. The COMM has initially foreseen that the min. tax rates would be defined by an implementing regulation with the consent of the EP.	
<b>6. Focus on European added value</b>	FTT is a text-book example of a tax whose implementation can be better achieved at EU level (or global level) due to the high mobility of its base.	
<b>7. Subsidiarity principle</b>	The FTT is not a 'European Tax' and arising OR would rather constitute a revenue sharing arrangement.	
<b>8. Limit political transactions costs</b>	Given its multiple objectives in relation to financial discipline, the popularity of such tax and little administrative costs or changes, the political transaction costs of the FTT could be considered low.	

## Bank Levy

<b>1. Equity/Fairness</b>	Depending on its design, and in particular whether it would concern the banks and financial institutions of all or only some Member States, such a tax-based resource could well fulfil the criteria of fairness and equity.	
<b>2. Efficiency</b>	The levy would be a gain in efficiency in the functioning of the Banking Union: it would create a level playing field in the area of taxation through the harmonisation of accounting rules.	
<b>3. Sufficiency &amp; Stability</b>	The revenues will depend of the design of the levy.	
<b>4. Transparency &amp; Simplicity</b>	Bank levy is fully transparent for its origin and its use.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	The origin and purpose of such own resource would be clear and would refer to well framed accounting rules.	
<b>6. Focus on European added value</b>	The Bank levy is fully linked to the European policy for increasing banks' resilience.	
<b>7. Subsidiarity principle</b>	It fulfils the principle of subsidiarity in the sense that it would be created at the adequate level of action in a single currency union.	
<b>8. Limit political transactions costs</b>	The possibility of reaching a consensus on such option, the prospects are very limited in the short run. But in the medium-term, perspective of a reform of the whole system of own resources, it may make sense to move from the financing of a Fund with risk specific fees to a financing based on corporate income tax or on added value.	

## EU VAT reformed

<b>1. Equity/Fairness</b>	Equity is ensured by the reduction of the call rate of the VAT-based own resource for a group of MS, in order to balance its regressive nature. However, this provision aims at equity and fairness between MS, not between EU taxpayers.	
<b>2. Efficiency</b>	The reformed system is simpler, more transparent and more efficient. Nevertheless, calculation remains cumbersome .	
<b>3. Sufficiency &amp; Stability</b>	The share of the revenue accruing from the VAT-based own resource would be fixed by the call rate or the fixed rate applied to the VAT base. The VAT-based own resource is considered a reliable source of revenue with limited volatility.	
<b>4. Transparency &amp; Simplicity</b>	The calculation of the theoretical VAT-base will be simplified.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	The VAT-based OR is approved by the MS in accordance with their respective constitutional requirements, is subject to EP scrutiny, to the Court of Auditors audits and to COMM services control. Nat. Parliaments are only involved in the real VAT collected revenue for the national budgets.	
<b>6. Focus on European added value</b>	The use of the actual VAT receipts in the new calculation method, instead of the current theoretical VAT base, would have created a stronger link with EU policies, and probably increased the awareness of the costs of the UE for citizens.	
<b>7. Subsidiarity principle</b>	Based on actual VAT proceeds, it would have had a more cost-effective implementation since the national collection system is already in place and the calculation are simplified, thereby reducing administration costs.	
<b>8. Limit political transactions costs</b>	Since VAT is collected within a well-established EU harmonised legal basis, political transaction costs can be considered to be low. The European Council (Feb.2013) already expressed its support to the revision of VAT based OR, and this shows interest for a future OR based on VAT.	

## Seigniorage

<b>1. Equity/Fairness</b>	The distribution of income from seigniorage is based on a specific key: the ECB capital key, which reflects each country's share in the total population and GDP of the EU.	
<b>2. Efficiency</b>	The technical calculations for this revenue stream being in place, implementation could be relatively straightforward. However, it would therefore require that an equivalent amount be statistically built for non-EA MS, or a differentiated treatment, which would probably increase the complexity in the system.	
<b>3. Sufficiency &amp; Stability</b>	The total amount of income from seigniorage has been rather volatile in recent years and it could only play a role as an own resource combined with others.	
<b>4. Transparency &amp; Simplicity</b>	The administration of such a tax is simple as its revenue is already collected centrally. Introducing for non-EA countries could introduce complexity.	
<b>5. Democratic accountability &amp; budgetary discipline</b>	ECB is independent from political influence and seigniorage revenues are therefore a given and do not depend on budgetary decisions.	
<b>6. Focus on European added value</b>	It has a direct link to the monetary union, but would require adjustments in relation to non-Euro members.	
<b>7. Subsidiarity principle</b>	The subsidiarity principle would logically suggest that central banks profits are allocated at the federal level. This is relevant for the Euro area but more difficult to justify for the EU as a whole.	
<b>8. Limit political transactions costs</b>	As Treaty change would be needed, the political transaction costs are high. Opposition of national central banks would be strong.	

## Annex VIII — Excerpt from the draft budget 2017 — the diversity of the financing side of the EU budget

### B. GENERAL STATEMENT OF REVENUE BY BUDGET HEADING

#### REVENUE —

Figures

Title	Heading	Budget 2017	Budget 2016	Outturn 2015
1	OWN RESOURCES	133 188 534 955	140 919 477 297	130 738 028 247,59
3	SURPLUSES, BALANCES AND ADJUSTMENTS	p.m.	1 349 116 814	8 031 205 136,60
4	REVENUE ACCRUING FROM PERSONS WORKING WITH THE INSTITUTIONS AND OTHER UNION BODIES	1 429 672 742	1 348 027 707	1 328 550 809,26
5	REVENUE ACCRUING FROM THE ADMINISTRATIVE OPERATION OF THE INSTITUTIONS	70 240 866	55 455 129	563 178 944,11
6	CONTRIBUTIONS AND REFUNDS IN CONNECTION WITH UNION AGREEMENTS AND PROGRAMMES	60 000 000	60 000 000	4 197 795 189,34
7	DEFAULT INTEREST AND FINES	120 000 000	123 000 000	1 703 065 168,67
8	BORROWING AND LENDING OPERATIONS	5 192 000	5 217 537	42 413 817,62
9	MISCELLANEOUS REVENUE	25 001 000	25 001 000	19 392 981,26
	<b>Total</b>	<b>134 898 641 563</b>	<b>143 885 295 484</b>	<b>146 623 630 294,45</b>

#### TITLE 1 — OWN RESOURCES

Figures

Title Chapter	Heading	Budget 2017	Budget 2016	Outturn 2015
1 1	LEVIES AND OTHER DUTIES PROVIDED FOR UNDER THE COMMON ORGANISATION OF THE MARKETS IN SUGAR (ARTICLE 2(1)(a) OF DECISION 2014/335/EU, EURATOM)	124 700 000	124 700 000	123 717 167,37
1 2	CUSTOMS DUTIES AND OTHER DUTIES REFERRED TO IN ARTICLE 2(1)(a) OF DECISION 2014/335/EU, EURATOM	20 000 500 000	18 465 300 000	18 606 636 770,66
1 3	OWN RESOURCES ACCRUING FROM VALUE ADDED TAX PURSUANT TO ARTICLE 2(1)(b) OF DECISION 2014/335/EU, EURATOM	19 376 814 450	18 812 783 576	18 268 893 143,27
1 4	OWN RESOURCES BASED ON GROSS NATIONAL INCOME PURSUANT TO ARTICLE 2(1)(c) OF DECISION 2014/335/EU, EURATOM	93 686 520 505	103 516 693 721	94 008 966 506,53
1 5	CORRECTION OF BUDGETARY IMBALANCES	0	0	-270 185 340,24
1 6	GROSS REDUCTION IN THE ANNUAL GNI-BASED CONTRIBUTION GRANTED TO CERTAIN MEMBER STATES	p.m.	p.m.	0,—
	<b>Title 1 — Total</b>	<b>133 188 534 955</b>	<b>140 919 477 297</b>	<b>130 738 028 247,59</b>

#### TITLE 7 — DEFAULT INTEREST AND FINES

Figures

Title Chapter	Heading	Budget 2017	Budget 2016	Outturn 2015
7 0	DEFAULT INTEREST AND INTEREST ON FINES	20 000 000	23 000 000	109 059 444,10
7 1	FINES AND PENALTIES	100 000 000	100 000 000	1 594 005 724,57
	<b>Title 7 — Total</b>	<b>120 000 000</b>	<b>123 000 000</b>	<b>1 703 065 168,67</b>

## CHAPTER 7 0 — DEFAULT INTEREST AND INTEREST ON FINES

Figures

Title Chapter Article Item	Heading	Budget 2017	Budget 2016	Outturn 2015	2015/2017
7 0	DEFAULT INTEREST AND INTEREST ON FINES				
7 0 0	<b>Default interest</b>				
7 0 0 0	Default interest in respect of own resources made available by the Member States	5 000 000	5 000 000	22 566 266,97	451,33 %
7 0 0 1	Other default interest	p.m.	3 000 000	423 965,88	
	<i>Article 7 0 0 — Subtotal</i>	5 000 000	8 000 000	22 990 232,85	459,80 %
7 0 1	<b>Interest related to fines and penalty payments</b>	15 000 000	15 000 000	86 069 211,25	573,79 %
7 0 2	<b>Interest on deposits in the framework of the European Union's economic governance - Assigned revenue</b>	p.m.	p.m.	0,—	
7 0 9	<b>Other interest</b>	p.m.			
	<b>Chapter 7 0 — Total</b>	<b>20 000 000</b>	<b>23 000 000</b>	<b>109 059 444,10</b>	<b>545,30 %</b>

## CHAPTER 7 1 — FINES AND PENALTIES

Figures

Title Chapter Article Item	Heading	Budget 2017	Budget 2016	Outturn 2015	2015/2017
7 1	FINES AND PENALTIES				
7 1 0	<b>Fines, periodic penalty payments and other penalties in connection with the implementation of the rules on competition</b>	100 000 000	100 000 000	1 439 608 863,28	1439,61 %
7 1 1	<b>Penalty payments and lump sums imposed on a Member State for not complying with a judgment of the Court of Justice of the European Union on its failure to fulfil an obligation under the Treaty</b>	p.m.	p.m.	153 278 000,00	
7 1 2	<b>Fines imposed for fraud and irregularities which are damaging to the Union's financial interest</b>	p.m.			
7 1 3	<b>Fines in the framework of the European Union's economic governance – Assigned revenue</b>	p.m.	p.m.	0,—	
7 1 9	<b>Other fines and penalty payments</b>				
7 1 9 0	Other fines and penalty payments - Assigned revenue	p.m.			
7 1 9 1	Other non-assigned fines and penalty payments	p.m.	p.m.	1 118 861,29	
	<i>Article 7 1 9 — Subtotal</i>	p.m.	p.m.	1 118 861,29	
	<b>Chapter 7 1 — Total</b>	<b>100 000 000</b>	<b>100 000 000</b>	<b>1 594 005 724,57</b>	<b>1594,01 %</b>

## CHAPTER 9 0 — MISCELLANEOUS REVENUE

Figures

Title Chapter Article Item	Heading	Budget 2017	Budget 2016	Outturn 2015	2015/2017
9 0	MISCELLANEOUS REVENUE				
9 0 0	<b>Miscellaneous revenue</b>	25 001 000	25 001 000	19 392 981,26	77,57 %
	<b>Chapter 9 0 — Total</b>	<b>25 001 000</b>	<b>25 001 000</b>	<b>19 392 981,26</b>	<b>77,57 %</b>

### Article 9 0 0 — Miscellaneous revenue

Figures

Budget 2017	Budget 2016	Outturn 2015
25 001 000	25 001 000	19 392 981,26

**Remarks**

**This article is intended to receive miscellaneous revenue.**

European Parliament	1 000
Council	p.m.
Commission	25 000 000
Court of Justice of the European Union	p.m.
Court of Auditors	p.m.
European Economic and Social Committee	p.m.
Committee of the Regions	p.m.
European Ombudsman	p.m.
European Data Protection Supervisor	p.m.
European External Action Service	p.m.
<b>Total</b>	<b>25 001 000</b>

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