EUROPEAN FILE

HOW AND WHY YOU PAY

The European Community budget

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At ECU 45 000 million, the 1989 European Community budget represents scarcely 1% of the combined gross national product (GNP) of the 12 Member States. This is a very small amount in comparison with the ECU 2 500 million which is the sum of the 12 national budgets.[1] Despite its modest size the Community budget has been the subject of fierce controversy, not only between the European Parliament and the Council of Ministers but also between the Member States. All of that was changed, however, by the reform decided at the Brussels European Council in February 1988, which was endorsed in June 1988 by a series of decisions and an agreement between the Community institutions. The principal elements of this budgetary reform:

- ☐ The Community has been given additional resources to enable it to meet the obligations arising from the Single Act, which supplemented the European Treaties with a view to the establishment of the large market of 1992.

- ☐ To counterbalance this, the planning of overall expenditure is the subject of an agreement between the Community's various institutions. This endorses, on the one hand, the priority given to policies for economic and social cohesion (including the gradual doubling of the European structural Funds – social, regional and agricultural) and, on the other hand, the introduction of a system of budgetary discipline which can effectively control expenditure, notably by providing for a series of ceilings for the 1988-92 period.

- ☐ Finally, the burden of financing the Community has been more fairly spread.

The finances of the European Community are, quite rightly, subject to democratic control: by the European Parliament and, through it, by public opinion. Each Community citizen has the right to know how this money is collected, what it is spent on and what procedures are involved. Some brief answers to these questions are provided in this file.

Revenue: new resources, limited and better balanced

The Community is financed by its own resources. These were increased in 1988 and their future growth limited by a global ceiling.

The European Coal and Steel Community (ECSC), founded in 1951 by the Treaty of Paris, has always had its own operational budget (ECU 329 million in 1989). From the beginning, it was financed by an early form of European tax, a levy (set at 0.31% in 1989) on the value of the production of coal and steel firms. In contrast, the European Economic Community (EEC) and the European Atomic Energy Community (Euratom), founded by the Treaties of Rome in 1957, were financed at first by national contributions, based mainly on the gross domestic product of

[1] This file replaces our No 17/86. ECU 1 (European currency unit) = about £ 0.65, Ir£ 0.77 or US$ 1.03 (at exchange rates current on 29 May 1989).

Member States. The Treaties did, however, provide for these contributions to be replaced by the Community's own resources. A decision to that effect was taken in 1970, making over resources which, though collected in the main by Member States, belong to the Community as of right. Since the reforms introduced in 1988 to rationalize, supplement and make fairer the system of own resources, a ceiling has been placed on their overall total. A global ceiling of 1.2% of the Community's total gross national product (GNP) was set for as long as the decision of 24 June 1988 on own resources continues to apply. Applicable to payment appropriations, this financial ceiling is also broken down into intermediate annual ceilings: 1.15% in 1988, 1.17% in 1989, 1.18% in 1990, 1.19% in 1991. In addition, a global ceiling of 1.3% of the total Community GNP is envisaged for commitment appropriations.

Revenue for the Community's general budget includes:

- ☐ Customs duties on products imported from outside the Community. This follows logically from the abolition of customs duties between the Member States and the adoption of a common customs tariff *vis-à-vis* external countries. Merchandise is imported throught the best-situated ports, railway depots, etc., even if it is destined for another Member State, whether in its original condition or following processing. To whom does the customs revenue from these imports rightly belong? As the question could not be answered, it made sense to declare it common property. This was done, in stages, by the six founding members of the Community between 1971 and 1975.

- ☐ Agricultural levies, traditionally charged at the external frontiers of the Community in order to bring the price of various imported foodstuffs up to the Community level. These levies do not bar products from Community markets. They only safeguard the future of Community farming by preventing possible distortions of competition due to cheap imports. To these can be added levies on sugar and isoglucose, created to limit surplus production in these sectors by making European producers bear the resulting costs.

- ☐ A proportion of the value-added tax base, determined in a uniform manner according to Community rules. This proportion, set at 1% in 1970, was raised to 1.4% in 1985 and will remain at this level until 1992. However, in order not to penalize countries (such as Portugal, Greece, Ireland and the United Kingdom) where private consumption represents a very sizeable share of national wealth, the 1988 reforms set a limit of 55% of GNP on the VAT base: a country where this base represents 70% of GNP will pay only on 55%. In addition, under the terms of their acts of accession to the Community, Spain and Portugal will until 1991 receive decreasing compensation for the fact that they will take time to draw the full benefit from their entry into the Community.

- ☐ A new resource (the 'fourth resource') created in 1988 and based on GNP. Revenue provided in this way is a function of a rate applied to the combined GNP of all the Member States. The rate is determined every year in the budgetary procedure (0.0924% for the 1989 budget), taking account of all other revenue. Each Member State contributes to this resource according to its GNP, and therefore according to its ability to pay. Note that the mechanism established in 1986 to reimburse to the United Kingdom 66% of the difference between its share of Community spending and its contribution to VAT revenue (justified on the grounds that the British benefit relatively little from Community spending on agriculture) has been improved. The United Kingdom contribution is now assessed according to the upper limit on VAT and to the GNP resource and this significantly reduces the size of the problem.

Finally, the June 1988 decision on Community resources provided for the possibility of new own resources, in the form of revenue from other taxes which, with the agreement of the Member States, could be instituted as part of European Community policies.

General Community budget: revenue forecast for 1989

	Million ECU	%
Customs duties	9 954	22.2
Agricultural levies	2 462	5.4
VAT	26 219	58.5
GNP resource	3 907	8.7
Miscellaneous	274	0.6
Balance from previous financial year	2 025	4.5
	44 841 (or 1.03% of Community GNP)	

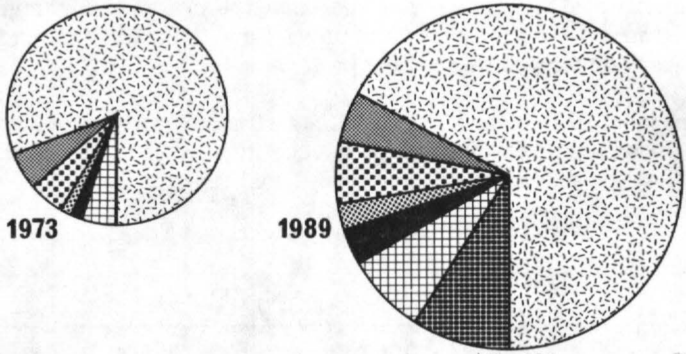
Expenditure: measured growth under financial discipline

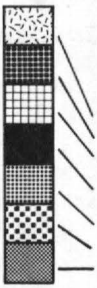
Figure 1 (page 6) compares expenditure in the Community's general budget for 1973 with that for 1989. Total expenditure increased tenfold in this period, while Community consumer prices quadrupled. To understand this development, we must remember that during this period the Community grew from six to 12 Member States. Moreover, the Community is not to be compared to a mature national State. Its expenditure is not simply additional to national government spending but rather takes the place of that expenditure whenever a joint initiative is seen to be more effective and less onerous than disparate national efforts. The Community's task now is to implement the objectives of the Single Act: to establish the large market of 1992 while strengthening Europe's technological base and its economic and social cohesion.

In comparison with the budgets of international organizations and even, to a certain extent, with those of Member States, the Community budget is devoted overwhelmingly to operational expenditure. Administrative costs take up less than 5% of

1. Development of the general Community budget, 1973-89

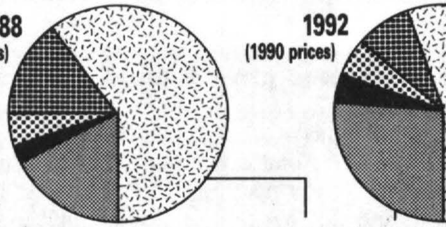
(actual expenditure) (payment appropriations)

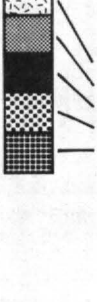




	million ECU 1973	million ECU 1989	% 1973	% 1989
Agriculture and fisheries	3 627	30 032	80.6	67.0
Regional policy	–	4 294	–	9.6
Social policy	249	3 232	5.5	7.2
Research, energy, industry, environment and transport	70	1 536	1.6	3.4
Development cooperation	61	1 032	1.4	2.3
Miscellaneous	250	2 562	5.5	5.7
Administration	248	2 153	5.5	4.8
Total	4 505	44 841		

2. Financial forecasts 1988-92 (commitment appropriations, million ECU)





	1988	1992
EAGGF Guarantee	27 500	32 000
Structural activities (Funds)	7 790	14 630
Multiannual appropriations (Research, IMPs)	1 210	2 610
Other policies	2 103	3 050
Other miscellaneous [1]	6 741	4 900
Total commitment appropriations	45 344	57 190
Total payment appropriations	43 820	54 250
Own resources as % of GNP	1.14	1.16

[1] Reimbursements to Member States, monetary reserve, administrative costs, etc.

Source: Community financial perspectives.

the total, despite the fact that running a multilingual Community requires an enormous amount of work and staff (for translation of documents, interpretation, etc.). In addition, the 'miscellaneous' expenditure in the illustration includes sizeable refunds to the Member States. Overall, more than 90% of the budget is devoted to economic, social and regional expenditure in member countries and in the Third World. Apart from spending on agricultural guarantees and some financing of the Community's Joint Research Centre, most expenditure is done on a shared-cost basis, with the Community subsidizing, according to strict criteria, programmes or projects submitted by Member States or by public or private bodies.

The 1988 reform, which became a reality with the decisions of 24 June and the agreement signed on 29 June between the European Parliament, the Council of Ministers and the European Commission, introduces a tighter budgetary discipline covering all categories of expenditure. To this end:

- A financial perspective for the 1988-92 period, jointly adopted, ensures a more balanced and controlled development of expenditure, by determining certain financial targets which also constitute global and sectoral ceilings (see page 6, Figure 2).

- A series of measures have been taken to control spending on agriculture: limiting the annual rate of growth of price guarantee spending to 74% of the growth of GNP; systematic depreciation of the book value of agricultural stocks; strengthening the system of 'stabilizers' to limit the financial intervention of the Community whenever a production ceiling is exceeded; the annual inclusion in the budget of a monetary reserve, in the form of provisional credits, to deal with major and unforeseen fluctuations in the dollar/ecu rate of exchange.

- Further measures were adopted at the same time to control the growth of other expenditure: a reference framework to be fixed annually for other 'obligatory' spending which, like agricultural guarantees, honours legal commitments to third parties (for example, aid to developing countries which have signed cooperation agreements); ceilings based on the financial perspective for 'non-obligatory' spending to develop Community activities (29% of payment appropriations in 1989).

With an overall increase in payment appropriations of 6.1% over 1988, the 1989 budget is the first to implement the principal features of the 1988 financial reforms. An inspection of its main headings reveals a number of important developments.

- Agriculture and fisheries absorbed 69% of Community spending in 1988; in 1989 they account for only 67%, of which farm price guarantees take 60%. The agricultural share of the budget continues to be sizeable, partly because in this area Community financing has effectively taken over from national financing. Nevertheless, it has become necessary to restrain agricultural spending. The reasons for its growth in recent years are well known: the success of the common agricultural policy, in terms of increasing productivity and guaranteeing previously uncertain supplies, finally ran up against the limits of the market. As exports and internal consumption grew more slowly than production, structural surpluses built up, while spending on support for exports, to compensate for the differences between Community and world prices, increased. The 1988 financial reforms, which are concurrent with the reform of the common agricultural policy to obtain a better mix of supply and demand and a reduction of the gap between European and world prices, will provide for more effective control of this spending.

- ☐ The 1989 budget is characterized by a major increase (+ 22% in payment appropriations) in allocations to the structural Funds – Regional Fund, Social Fund and the 'Guidance' section of the Agricultural Fund. To reinforce Community economic and social cohesion in anticipation of the large market of 1992, the Single Act amending the European Treaties provided for greater coordination of the activities of these Funds and the European Council decided on a doubling of their resources between 1987 and 1993.

- ☐ Regional policy absorbs 9.6% of expenditure in 1989 as against 7.1% in 1988. There was no regional spending at all in the 1973 budget. It is only since 1975 that the European Regional Development Fund has been in existence, helping poorer regions and areas in decline by co-financing development programmes, infrastructural, industrial and service investment, and various schemes to encourage business initiatives.

- ☐ There has been a large increase in budget appropriations for the integrated Mediterranean programmes (IMPs). These are for stimulating the development of the Mediterranean regions in Greece, Italy and France in order to help them cope with the effects of the enlargement of the Community to include Spain and Portugal. For this purpose ECU 4 100 million is to be provided in the budget between 1986 and 1993.

- ☐ Social policy accounts for 7% of total spending. Most of this is spent through the European Social Fund which co-finances training and retraining schemes and aid for recruitment. Special attention is paid to young people, to the long-term unemployed and to regions affected by industrial decline. In addition, there is an increased allocation for young people, particularly for exchange programmes such as Erasmus, Comett and 'Youth for Europe'. In this way the Community demonstrates its willingness to take account of the social dimension of the large market of 1992.

- ☐ Certain sectors continue to receive scant funding. Although research (2.7% of expenditure); industry, innovation and the internal market (0.3%); energy (0.3%); and the environment (less than 0.1%) have increased their appropriations, funds allocated to transport (less than 0.1%) have decreased. The financial perspective adopted in 1988 envisages a doubling, between now and 1992, of commitment appropriations for multiannual programmes (research and IMPs). Strengthening the cohesion and technological base of the Community must go hand in hand with the establishment of the large market.

- ☐ Development cooperation, to which 2.3% of expenditure is allocated, shows an 18% increase in funds over 1988. This expenditure is intended mainly for food aid and for assistance to Mediterranean, Asian and Latin American countries. Financial and technical aid, of a roughly equivalent amount, is provided under the Lomé Convention for 66 African, Caribbean and Pacific countries (ECU 7 400 million between 1985 and 1990). This aid is financed outside the framework of the Community budget through the European Development Fund, which is still constituted from national contributions.

The decision-making process

The Community's annual general budget is established by a complex process. This extends over more than half the previous year and involves the Commission, the European Parliament and the Council of Ministers.

- ☐ First the European Commission draws up a preliminary draft budget. This takes account of the needs of the Community and its institutions, estimated revenue, and, since 1989, multiannual financial perspectives approved by the European Council and the European Parliament. The preliminary draft budget goes before the Council of Ministers which adopts or amends it by qualified majority (54 votes out of 76, with Germany, France, Italy and the United Kingdom having ten votes each, Spain eight, Belgium, Greece, the Netherlands and Portugal five each, Denmark and Ireland three each and Luxembourg two). The Council's draft budget is then debated by the European Parliament, which can propose modifications of 'obligatory expenditure' or vote amendments to 'non-obligatory' expenditure.

- ☐ On its second reading of the budget, the Council of Ministers must have a qualified majority to accept any modifications proposed by the European Parliament which would increase obligatory expenditure. Other modifications require a qualified majority to reject them (here we speak of a negative majority); the same holds true for amendments dealing with non-obligatory expenditure. These amendments, if rejected by a qualified majority, can be reinstated by the Parliament. In this respect, and within certain limits – which are now a function of the ceilings introduced in 1988 by the financial perspectives jointly adopted by the institutions – the Parliament has the final word. At the end of this stage, unless the Parliament rejects the budget as a whole, the President of the Parliament declares it adopted.

It was the change-over to a system of own resources outside the control of national parliaments that made it necessary, for obvious democratic reasons, gradually to strengthen the European Parliament's budgetary powers. This was done mainly on the basis of two treaties, signed in 1970 and 1975. The power of decision with regard to the budget is now shared between the Council and the Parliament. They constitute the two arms of the budgetary authority. Besides the last word on non-obligatory expenditure and the right to reject the budget, the Parliament also has sole power to give discharge to the Commission for its execution, having first checked whether the budget was spent in accordance with the regulatory framework and the decisions of the budgetary authority.

Verification of the legality and regularity of Community revenue and expenditure, and of its proper management, is entrusted to an independent institution established in 1975, the Court of Auditors of the European Communities. A series of initiatives is under way to prevent and eliminate fraudulent and irregular practices by certain operators seeking to benefit from Community subsidies. The European Commission, which has established a special unit to fight fraud, has proposed various measures to the Council of Ministers and asked for a strengthening of cooperation between the Member States, which in many instances are responsible for payments and supervision 'on the ground'.

The limitations of the budgetary approach

An analysis of the budget tells us much about how European integration is proceeding — but it does not give the full picture:

- ☐ Firstly, a number of financial operations undertaken by the Community are outside the budget. These include the European Development Fund, mentioned above, as well as various borrowing and lending activities by the European Commission and the European Investment Bank. Finance raised on capital markets is used to support projects in the Third World as well as coal and steel modernization and restructuring, modernization in the energy sector, the development of small and medium-sized businesses, and priority investments relating to the regions, the environment, communications and advanced technologies. A total of ECU 10 900 million was lent for these purposes in 1988 (equivalent to 25% of that year's budget).

- ☐ In addition, the European Commission is developing a role in 'financial engineering': helping the private sector to create financial instruments which correspond to the needs of companies, particularly small and medium-sized enterprises (SMEs), while also furthering some of the principal objectives of the Community: unification of the internal market, technological progress, employment creation, improved industrial competitiveness, integration of peripheral regions, etc. Thus the Community has undertaken to promote European risk capital activities and assistance for innovatory projects by SMEs. Other types of assistance are intended to help finance high technology and major transport infrastructure projects.

- ☐ Finally, figures never tell the whole story. Apart from borrowing and lending, there is a whole range of activities that involve no expenditure and so are not mentioned in the budget. The creation of a common market between the 12 Member States and its complete integration in the framework of the large single market of 1992 will encourage the expansion of trade, increased competition, economies of scale and improved productivity. It will also give Europeans greater weight in a world dominated by continental powers. Clearly all of that — which cannot be itemized in a budget — is worth more to industry, workers and consumers than are the meagre budgetary resources allocated to industrial, innovation and research policies (between them, these policies received only 3% of appropriations in 1989).

Some conclusions

The 1989 budget marks an important turning point in the budgetary approach of the Community and demonstrates its willingness to draw up a budget conforming to the objectives of the Single Act. The budgetary reform of 1988 effectively enabled a number of uncertainties, which had been hanging over the future of the Community, to be removed.

☐ The Community budget can no longer be accused of being concerned only with agriculture. The reform has introduced a general budgetary discipline and a more equitable distribution of expenditure in favour of other sectors requiring Community action in the context of the completion of the internal market of 1992. The process of budget rationalization is well under way. The budget appropriations for the new policies envisaged by the Single Act (structural activities, research, internal market, environment), which account for 24% of total expenditure, may still appear too small, but their growth is programmed into the 1988-92 financial projections. It should also be remembered that, in most areas, Community action complements national initiatives.

☐ The reform provides the Community with sufficient resources to implement its policies, with prudent limits extending until 1992. The mechanisms employed take account of the economic situation of the Member States and allow for a more equitable distribution of the burden of financing the Community budget.

☐ Finally, the Community no longer has to face recurrent crises which question the credibility of its institutions – as happened during the first half of 1988 when, deprived of a budget due to disagreement between the Parliament and the Council, it operated each month on a 'provisional twelfth' of the previous year's allocations. The budgetary process has now been rationalized and the Community may calmly programme its activities as 1992 approaches ■

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