COMMISSION OF THE EUROPEAN COMMUNITIES

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FUTURE FINANCING OF THE COMMUNITY

(Communication from the Commission to the Council)

The Commission proposed in May 1983 that under the 1970 Decision on own resources a new Community decision-making procedure should be instituted for setting the rate of call-up applicable to the basis of assessment for VAT.

The procedure would be operated for the first time before the setting of a VAT call-up rate above 1.4 %.

The Commission's proposal received the support of the European Parliament, with the qualification that the matter must be dealt with in the framework of the powers pertaining to national ratification procedures. From the Council discussions it emerged that the overwhelming majority of the Member States wished to continue the principle of a ceiling rate laid down in the 1970 Decision and the requirement that any increase in the ceiling rate is to be agreed by the Member States unanimously and ratified by the national Parliaments.

This being so, the Commission would now make the point that the Community is consequently in the same position as at the time of the 1970 Decision ; the Community has accordingly to set a new ceiling on the increase of VAT own resources.

The 1970 Decision gave the Community financial security for thirteen years.[1] A decision of like scope is called for now, taking account of a number of considerations that did not apply when the 1970 Decision was taken.

1. Future development of the Community Budget in the context of budget discipline

Raising the own resources ceiling is this time part and parcel of a set of arrangements proposed by the Commission for containing farm spending and establishing strict budget discipline generally.

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[1] Whereas in 1981 the VAT call-up rate was still the same as in 1979, viz. 0.78, in 1982 it suddenly moved to over 0.9. Since 1983 the Community Budget has been up against the own resources ceiling, as the combined result of farm spending and offset payments to correct the imbalances in the distribution of budget charges. (Had it not been for the offset payments the 1983 call-up rate would have been 0.875.)

The strict budget management guaranteed by the decisions which the Council takes on the basis of the Commission's proposals will ensure that the new resources are of a permanent nature by enabling the growth of the Community Budget to be kept within bounds.

At the same time the European Council's decision on the future financing of the Community must show a dynamic approach and offer a real prospect of further development in the medium term.

For there are cases where joint action by the Member States is more effective and economical than action by the Member States is more effective and economical than piecemeal national measures. With all due respect for the constraints on public spending throughout the Community, the financing system of the Community must therefore be given sufficient flexibility to take on further developments in line with these economy requirements, particularly as they mean in practice that the demands on the national Budgets are less.

2. <u>Enlargement</u>

The raising of the own-resources ceiling must also enable the Community Budget to cover the financial implications of Spanish and Portuguese accession.

The annual profile of the budgetary effects of enlargement cannot be determined at the present stage of the negotiations with Spain and Portugal. To start with the increase in Community expenditure will stem mainly from higher structural expenditure for the benefit of the acceding countries and the Mediterranean regions of the Community; later on enlargement might involve a <u>net</u> increase in the Community Budget of 0.1-0.2% of VAT.

3. <u>Rate of growth of own resources</u>

Prudence demands that we should not bank on a real growth rate in Community GDP of more than 2.5 % p.a. over the coming years.

The average annual growth in the VAT basis of assessment should not exceed that in GDP. Moreover, the trend in movement of the other revenues is sluggish: in fact in real terms their value has actually declined.[1]

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[1] The traditional own resources (agricultural levies, sugar and isoglucose levies, customs duties) rose in face value by an average 6.8% p.a. in the period 1978-83, while during the same period GDP implied prices rose by 8.9% p.a. The real value of the traditional own resources thus fell by an average 1.9% p.a. during those five years.

In 1978 customs duties and the other common policy-related revenues accounted for 45% of available own resources, but in 1984 the figure is only 42%.

This trend can be expected to continue, and indeed to gather pace, in the years ahead. Most customs duties are bound in GATT and come under a dismantling schedule which could be speeded up in accordance with the progress of world efforts to liberalize international trade.

As for the agricultural levies, they are a particularly erratic source of finance, whose yield will be adversely affected by the implementation of the Commission's proposed CAP reforms.

Care must be taken therefore not to equate an increase in the Community Budget with an increase in the VAT revenues required. The relative diminution in the other resources automatically involves, for a given real increase in the Budget, a faster increase in the VAT revenues called up. Thus it has been estimated that tariff dismantling and the fall in the agricultural levies consequent on CAP reform could mean, at a time-scale of 10-15 years, a 0.2% increase in the VAT call-up rate merely to maintain the real value of available own resources.

4. <u>Time needed</u>

To gain the Council's agreement to a proposal for going above the own-resources ceiling, and after that to obtain ratification by the national Parliaments (twelve of them after enlargement), will take at least two years. This cuts two years off the period during which the higher own resources ceiling will allow trouble-free Community budgeting.

Moreover the credibility of the Community system would suffer severely if the national Parliaments had to be constantly applied to in order to obtain the wherewithal to go ahead with the common venture.

In the two financial years that will elapse between the exhaustion of own resources within the 1% ceiling and the advent of the new resources Budget growth will be completely straitjacketed. Hence there is bound to be an accumulation of commitments and deferments of expenditure which will have to be honoured later. This is inevitable even if the Commission's proposals for the reform of the CAP are adopted in full in principle by the Brussels European Council in March,

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for even then it would still take time to turn the decisions-in-principle into operational regulations, and time again for the regulations to have their full budgetary impact. So it could be that the Community Budget will have to be temporarily increased for so long as it takes to implement the arrangements for properly containing farm spending. This factor, which may be discounted in a long-term context, would become very relevant indeed if the new own-resources ceiling were not consonant with the long-term context and in fact only afforded the Community a breathing-space.

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5. In view of the foregoing the Commission is proposing that the Council today take a decision of like importance to that of 1970, raising by one point the maximum rate determining the revenue from value-added tax which may be assigned to the Community.

The Commission is of the opinion that this increase of the ceiling rate from 1 to 2% of the basis of assessment for VAT would give the Community secure financing for long enough to cover the whole transitional period of its enlargement to include Spain and Portugal.

In asking the European Council to give the Community this financial security - monitored in accordance with the budget discipline rules - it is thus asking the Member States to have the same degree of confidence in Europe as they did in 1970.

It is not asking them to accept the principle of automatic, regular increases in Community revenue-generation.

By deciding to make available to the Community a certain range of potential resources the Member States will not be authorizing their deployment; the actual expenditure and revenue of the Community will be determined through the annual Budget procedure, strictly within the framework of the rules on budget discipline proposed by the Commission.

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[1] During that period it is also necessary to allow for the effects, at the appropriate time, of budgetizing the EDF.

Annex

Development of the Community Budget and funding thereof

(some significant points)

1978-83

Total expenditure

As a % of Community GDP, 1978	0.79%
1983	0.93%
As a % of national Budgets, 1978	2.6%
1983	2.8%
Real annual average growth rate	5.8 %

VAT

Rate of real annual average growth in basis of assessment for VAT 1979-83	1.9%
Rate of real annual average growth in VAT revenues collected 1979-83	8.9%
VAT call-up rate 1979	0.7781
VAT call-up rate 1983	0.9980

Other resources

Rate of real annual average growth in agricultural resources	-8.0%
Rate of real annual average growth in total customs duties	+0.8%
Rate of real annual average growth in total other resources	-1.9%