European Communities

EUROPEAN PARLIAMENT

Working Documents

1980 - 1981

5 January 1981 DOCUMENT 1-772/80

REPORT

drawn up on behalf of the Committee on Budgets

on the Community's own resources

Rapporteur: Mr A. SPINELLI

English Edition

PE 64.634/fin.

By decision of 17 April 1980 the Bureau of the European Parliament authorized the Committee on Budgets to draw up a report on the Community's own resources.

This report was drawn up by the ad hoc Working Party chaired by Mr Spinelli and consisting of Mr Ansquer, Mr Arndt, Mr Barbi, Mr Nord and Mr J.M. Taylor.

The Committee on Budgets considered the ad hoc Working Party's draft report at its meetings of 28 May, 4 June, 11 and 24 September, 25 November and 3 December 1980.

It adopted the report by 21 votes to 5 with 2 abstentions at its meeting of 3 December 1980.

Present: Mr Lange, chairman; Mr Notenboom and Mr Spinelli, vice-chairmen; Mr Adonnino, Mr Aigner, Mr Ansquer, Mr Arndt, Mr Baillot, Mr Barbi, Mr Colla, Mr Fich, Mr Flanagan, Mr Forth, Mr Gouthier, Mrs Hoff, Mr R. Jackson, Mr Langes, Mr Motchane, Mr Newton Dunn, Mr Orlandi, Mr Pfennig, Mrs Pruvot (deputizing for Mr Nord), Mr Ryan, Mr Konrad Schön, Mrs Scrivener, Mr Simonnet, Mr J.M. Taylor and Mr Tuckman.

CONTENTS

A

The Committee on Budgets hereby submits to the European Parliament the following motion for a resolution, together with explanatory statement:

MOTION FOR A RESOLUTION

on the Community's own resources

The European Parliament,

- having regard to the Treaty establishing the European Economic Community, and in particular to Article 201,

- having regard to the Treaty establishing the EAEC, and in particular to Article 173,

- having regard to the Treaty establishing the ECSC, and in particular to Article 49,

- having regard to the communication from the Commission to the Council and the European Parliament on 'Financing the Community's budget: The way ahead' (COM(78) 531 fin.),

- having regard to the report of the Committee on Budgets (Doc. 1-772/80),

(a) Whereas the Community's general budget for 1980 amounted to 15,683 m EUA, in payment appropriations representing 0.80% of the Community's total GDP, 2.6% of the Member States' total budgets, of which 73.2% was utilized for expenditure under the EAGGF, Guarantee Section, 14.1% for expenditure on structures, 3.8% for operational expenditure, and 3.9% for expenditure on cooperation with developing countries;

(b) Whereas, apart from the general budget, the Community was responsible in 1980 for the management of:

- ECSC expenditure, from a parafiscal levy, amounting to 113 m EUA;
- borrowing and lending operations on the capital markets (ECSC, Euratom, NCI (1979), Community loans (1977)), amounting to 3,115 m EUA;
- the European Development Fund, from contributions from the Member States, amounting to 300 m EUA;

that is, an overall financial volume for 1980 of 3,528 m EUA, or 22.5% of the EEC budget;

(c) Whereas in 1980 the financing of the general budget broke down as follows:

- agricultural levies and sugar contributions, 14.1% of own resources, amounting to 2,223.7 m EUA;
- customs duties, 36.1%, amounting to 5,667 m EUA;
- VAT, 45.6%, amounting to 7,151 m EUA;
- miscellaneous revenues, 4%, amounting to 640.5 m EUA;

(d) Whereas the yield from VAT is restricted by the 1% ceiling on the rate on tax base applied by the Member States; that the yield from customs duties, because of the tariff reductions under GATT, will be growing at a progressively decreasing rate; and, lastly that the yield from agricultural levies, while it will fluctuate, will remain only a minor fraction of own resources;

(e) Whereas borrowing and lending operations, although they must be expanded, will necessarily be subject to limitations;

(f) Whereas, therefore, the ceiling on own resources available at present to the Community will very probably be reached in the 1981 budget, and it will accordingly be necessary to find new own resources soon in order to avoid a return to the system of national contributions;

(g) Whereas the alteration of the ceiling on own resources is conditional on a more rational and more economical restructuring of the Community budget;

1. Approves the conclusions and the recommendations submitted by the Committee on Budgets, which are contained in the ensuing paragraphs:

I. The size of the Community budget

2. Reaffirms its conviction, expressed on a number of occasions, that it is urgently necessary to bring agricultural policy expenditure under control in order to end the uncontrolled growth of spending under this heading and the creation of surpluses, and in order to allow a more equitable distribution of financial resources between the various Community policies;

3. Calls the attention of public opinion, of the Member States, and of all the Community institutions to the fact that the Community will have to extend the sphere of its responsibilities and assume new tasks and that the size of its budget must therefore be increased;

4. Confirms the conclusions of the MacDougall report, and in their light forms the opinion that Community structural and short-term economic expenditure will only have a significant influence if it accounts for a considerably higher percentage of the Community's gross domestic product;

5. Believes that, as a rule, such increases should proceed in step with the progressive transfer of responsibilities and would, therefore, involve the transfer of resources by the Member States to the Community, without thereby increasing the overall burden on the taxpayers,

II. Unity and comprehensiveness of the budget

6. Recalls that Article 199 EEC and Article 171 EAEC have established the principles of the unity (expenditure and revenue must be in balance) and the comprehensiveness (all revenue and all expenditure must be entered in the budget) of the Community budget;

7. Deplores the fact that until today resources deriving from borrowing and those intended for the European Development Fund remain outside the budget; and that, absurdly, some revenues are considered as negative expenditure; and requests that both these situations be ended as soon as possible;

8. Is of the opinion that parafiscal charges can be tolerated only exceptionally but should, in any event, be entered in the budget revenue;

9. Considers that the ECSC budget, which is separate from the Community budget and which is drawn up by different procedures from those applying for the general budget, should no longer retain this abnormal position.

III Improvements that can be made in the present system of own resources

10. Points out that the European Parliament has come down in favour of a reclassification of expenditure not directly related to the common agricultural policy with a view to ensuring greater transparency and objectivity in the distribution of budgetary resources.

11. Regards it as essential that the existing system of own resources be improved, to make it fully consistent with the principles of Community law and with the responsibilities of Community institutions;

12. Considers, therefore, that total harmonization of the VAT tax base must be undertaken speedily and preparations made for the subsequent harmonization of the rates, which is also needed if the remaining frontier checks on intra-Community trade are to be abolished;

13. Requests that, pursuant to the decision of 21 April 1970, after 1 January 1983, VAT should no longer be collected on the basis of statistical estimates, but on the basis of tax declarations, involving no additional administrative burdens, particularly for small and medium-sized undertakings, so that this source of revenue becomes a veritable Community VAT, parallel to the national VATs, because assessed on the same tax base, but levied at separate rates, independent of the national VAT rates;

14. Regards it as imperative that the Commission should have adequate supervisory bodies at its disposal , in the territory of the Member States;

15. Is convinced that implementation of the above principles will help to reduce negligence, fraud and tax evasion; to increase public awareness of the existence and progress of the Community; to eliminate the erroneous, but persistent, notion that the Community is financed from the exchequers of the Member States.

IV. The Community's loan policy

16. Restates the position it has held since 1975 in favour of increased use of loans, subject to the twin conditions that the loan policy shall be rationalized and that it should be under adequate control of the budgetary authority;

17. Is convinced that this development is necessary if productive investments and the convergence of the national economies are to be effectively promoted,

18. Is of the opinion that, to achieve these objectives, the Community's borrowing and lending operations should rapidly achieve an average annual total volume of 25% of the amount of the Community budget, exclusive of EIB operations;

19. Invites the Commission to examine the possibility of encouraging public savings through the issue, simultaneously throughout the Community finance markets, of Community bonds denominated in ECU, and looks forwards to proposals to this effect.

V. Financing of the Community budget in the short-term

20. Considers that the necessary additional finance can be injected in the short-term only by applying relatively rapid procedures and that, therefore, such injections must be restricted to more extensive use of existing sources of finance;

21. Rules out, at the same time, the use of Common Customs Tariff duties as an instrument of Community finance;

22. Is therefore of the opinion that, for the short term, raising the ceiling on VAT above the 1% limit remains the most appropriate measure in political, institutional and administrative terms, assuming that the Member States, in accordance with their respective constitutional requirements, agree to the amendment of Article 4(1), second paragraph, of the Decision of 21 April 1970 concerning the maximum rate of 1%;

23. Notes that the most advisable solution is the abolition of the ceiling on Community VAT;

VI. Redistribution through budgetary measures

24. Considers that, in order to introduce greater equity among the Member countries in the Community tax system, it is necessary to apply a corrective mechanism to the VAT which in its present form contains no elements of progressivity;

25. Is convinced that, in order to achieve a tangible increase in budget expenditure having a redistributive effect - with the prime aim of reducing per capita income inequalities and economic disparities between regions - it is necessary to introduce weightings for VAT transfers;

26. Proposes therefore:

(a) a weighting based on the different gross domestic products of the Community Member States expre ed in per capita purchasing power

- through a coefficient
  with redistributive effect based on the above- or below-average level of gross domestic product expressed in per capita purchasing power,

- this coefficient to be calculated in such a way that each Member State's deviation from the Community average is established, and then

- the value added tax amount for each individual Member State, expressed as 100, is increased or decreased by a tenth part of this deviation.

(b) a weighting based on the Member States' share of the Community's total population:

- through an additional coefficient based on the above- or below-average proportion of the total Community population figure,

- this coefficient to be calculated in such a way that each Member State's deviation from a notional average of 10% of the total population is established, and then

- the value added tax amount for each individual Member State, expressed as 100, is increased or decreased by a tenth part of this deviation.[1]

VII. Financing of the Community budget in the medium-term

27. Is convinced that, although the corrective mechanism envisaged in paragraphs 24-26 of the present resolution does introduce greater equity between the Member countries (taking each as a whole), it is not progressive in its impact on individual taxpayers; hence VAT and customs duties must not be allowed to remain the only taxes of a Community that aims to concern itself increasingly with equity in the economic, social and fiscal spheres;

28. Considers that following any Community harmonization of personal income tax, corporation tax and taxes on consumption (such as VAT), these taxes may form a new basis for the Community's own resources;

[1] See Annex II to the resolution

VIII. The decision-making machinery

29. In the knowledge that the growth of the Community's responsibilities, and hence of its revenue and expenditure, cannot take place without strong participation by all the political institutions , regards it as essential that an appropriate procedure be introduced for this participation;

30. Proposes, therefore, that in view of its responsibility before the Community's electorate, each newly elected European Parliament should, in the course of the first year following its election :

(a) consider with the Commission whether, and under what conditions, there should be a reallocation of responsibilities and financial resources between the Member States and the Community;

(b) if appropriate, adopt and forward to the other Institutions a draft joint declaration on the Community's financial needs and resources for the next five-year period;

31. Considers it essential that, by virtue of the financial autonomy of the Community, the Institutions should henceforth be able to amend or reinforce the own resources system themselves - and therefore invites the Commission to recommence the procedure for revision of Article 201 EEC initiated in 1973, taking account of the proposal annexed to this resolution.[1]

32. Believes that in this way the determination of the Community's new tasks and the consequent costs could become the central theme of future European electoral campaigns in which all the parties would necessarily take part; and that the debate on fiscal matters between the various Institutions would thus become a general political debate on the Community's objectives for the following five-year period.

IX. Conclusions

33. Requests that in its programme to be presented to the European Parliament the new Commission should:

- undertake above all to propose without delay the abolition of the 1% ceiling on the VAT yield (see paras. 22 and 23) and the VAT corrective mechanism (see paras. 24 to 26);

[1] See Annex I to the resolution

- undertake to present proposals for developing the loans policy in line with the wishes of the European Parliament (see paras. 16 to 19);

- include the coresponsibility levy in the budget revenue (see paras. 7 and 8);

- give precise details of the timetable for presenting proposals on:

  (a) complete harmonization of the basis of assessment and subsequently of VAT rates - see paragraph 12 above;

  (b) introduction of the declaration-based method of VAT collection - see paragraph 13 above;

  (c) supervision of collection of duties - see paragraph 14 above;

  (d) the issue of ECU-denominated Community bonds - see paragraph 19 above;

  (e) possible harmonization of the basis of assessment and of the rates of direct and indirect taxation - see paragraph 28 above;

- withdraw the 1973 proposal for an amendment of Article 201 EEC and introduce a new proposal in line with the decision-making mechanism suggested by the European Parliament - see paragraphs 30 to 32 above;

34. As regards the future use of the Community's own resources, undertakes to define the responsibilities which lie jointly or severally with the Community and the Member States;

35. Instructs its President to forward this resolution and the report of its committee to the Commission, the national Parliaments, the Council, and the Governments and Parliaments of Spain and Portugal.

ANNEX I

Existing Article 201	Text proposed by the Commission on 10.10.1973	Text proposed by the European Parliament
The Commission shall examine the conditions under which the financial contributions of Member States provided for in Article 200 could be replaced by the Community's own resources, in particular by revenue accruing from the common customs tariff when it has been finally introduced.	The Commission shall examine in what manner new resources may be allocated to the Communities.	The Commission shall examine in what manner the existing own resources must be changed or new resources may be allocated to the Communities.
To this end, the Commission shall submit proposals to the Council.	At least every five years the Council, after receiving a report from the Commission and consulting the Assembly, shall examine whether and in what manner new resources should be created.	Every five years the Council and Parliament, after receiving a report from the Commission, shall examine whether and in what manner the existing own resources should be changed or new ones created.
After consulting the Assembly on these proposals the Council may, acting unanimously, lay down the appropriate provisions, which it shall recommend to the Member States for adoption in accordance with their respective constitutional requirements.	On a proposal from the Commission and after unanimous agreement in the Council, the Assembly, voting by a majority of its members and three-fifths of the votes cast, may change the existing ceiling on own resources or create new resources.	On a proposal from the Commission and after unanimous agreement in the Council, the Assembly, voting by a majority of its members and three-fifths of the votes cast, may

VAT WEIGHTING MECHANISM

ANNEX II

Table 1

	Gross domestic product	± EEC average	coefficient
Belgium	4.68%	+ 23%	102.3%
Denmark	2.72%	+ 38%	103.8%
Germany	31.75%	+ 35%	103.5%
France	23.66%	+ 15%	101.5%
Ireland	0.63%	- 50%	95.0%
Italy	13.4 %	- 38%	96.2%
Luxembourg	0.17%	+ 21%	102.1%
Netherlands	6.34%	+ 18%	101.8%
United Kingdom	16.65%	- 22%	97.8%

Table 2	Share of population	deviation from 10%	coefficient
Belgium	3.79%	- 6.21%	99.4%
Denmark	1.97%	- 8.03%	99.2%
Germany	23.56%	+ 13.56%	101.4%
France	20.55%	+ 10.55%	101.1%
Ireland	1.26%	- 8.74%	99.1%
Italy	21.90%	+ 11.90%	101.2%
Luxembourg	0.14%	- 9.86%	99.0%
Netherlands	5.39%	- 4.61%	99.5%
United Kingdom	21.45%	+ 11.45%	101.1%

Table 3

The formulas combined

Belgium	101.7%
Denmark	103.0%
Germany	104.9%
France	102.6%
Ireland	94.1%
Italy	97.4%
Luxembourg	101.1%
Netherlands	101.3%
United Kingdom	98.9%

Table 4

Effect of formulas 1, 2 and 3 on the 1980 budget (in m EUA)

	Preliminary draft	coeff. 1	coeff. 2	coeff. 3 (1+2)
Belgium	304	311	302	309
Denmark	176	182	174	181
Germany	2,195	2,272	2,225	2,302
France	1,652	1,676	1,669	1,694
Ireland	57	55	57	54
Italy	729	702	738	711
Luxembourg	14	14	13	14
Netherlands	405	413	403	411
United Kingdom	1,162	1,136	1,175	1,149
	6,694	6,761	6,756	6,825

B

EXPLANATORY STATEMENT

At its meeting of 28 November 1979 the Committee on Budgets decided to set up an ad hoc Working Party to examine the question of the development of the Community's own resources.

This group, chaired by Mr Spinelli, vice-chairman of the Committee on Budgets, comprised the following members of the Committee on Budgets: Mr Ansquer, Mr Arndt, Mr Barbi, Mr Nord and Mr J.M. Taylor.

On the basis of a preliminary working document prepared by Mr Spinelli, the Working Party organized its work around six principal themes, each member of the party drawing up a working document on one of these themes:

- Mr Ansquer: 'an assessment of the present system of own resources for the Community' (PE 63.459/fin.),
- Mr Arndt: 'redistribution through budgetary measures' (PE 63.557/fin.),
- Mr Barbi: 'the ratio between Community and national financial resources' (PE 63.567/fin.),
- Mr Nord: 'the decision-making machinery for the Community's own resources' (PE 63.435),
- Mr Spinelli: 'new own resources for the Community' (PE 64.510),
- Mr Taylor: 'the Community's loan policy' (PE 63.761/fin.).

These documents are annexed to the present report and constitute its explanatory statement.

On the basis of the above documents Mr Spinelli drew up a motion for a resolution which was adopted by the Committee on Budgets on 3 December 1980.

The working party began its activities on 18 December 1979 and ended them on 30 April 1980. It held six meetings and heard statements from the Commissioner responsible for budgetary matters and several high-ranking officials of the Commission's economic and budgetary departments.

The working party drew notably on the following documents:

- the Commission's 'green paper' of 23 November 1978 entitled 'Financing the Community budget: The way ahead' (see Supplement 8/78 to the Bulletin of the European Communities),
- the study by a group of experts (the MacDougall group) of April 1977, entitled 'Report of the study group on the role of public finance in European integration'.

It should finally be recorded that the Working Party had intended to obtain statements from several European specialists in public finance, but the restrictions imposed by the budget situation at the beginning of the financial year 1980 (the system of provisional twelfths) made it impossible to arrange this hearing.

I.

the ratio between Community and
national financial resources

Draftsman: Mr BARBI

INTRODUCTION

1. This document draws on the ideas put forward in the working party's programme under the heading 'ratio between Community and national financial resources'.

2. Throughout its work the working party has been struck by the growing disparity between:

- the ambitious goals set for the Community in the Treaties and in the most recent statements by the Heads of Government of the Member States, notably at the Bremen Summit[1],

and

- the paucity of the financial resources currently available to the Communities and the reluctance of the Heads of Government to increase them.

3. It became apparent to the working party that the reasons for this disparity, which becomes more serious as the available resources are used up, are both political and technical and can be summarized as follows:

- the challenging (particularly since enlargement) of the objective of Community integration with consequent doubts as to how far the common policies should go;

- the persistence (and even hardening) of Member States' resistance to the transfer of sovereign powers to the Community, both at the level of national administrative bodies and of political authorities;

- a degree of disillusion at how little progress has been made towards economic convergence, despite the effects of the opening up of markets and of active redistribution policies;

- growing doubt as to the effectiveness of some existing Community policies, particularly the principal among them, the agricultural policy, which are often over-compartmentalized and pursued out of the main national and Community economic context.

- increased budgetary difficulties faced by the Member States as a consequence of the general economic trend since 1975.

---

1 Concerning strengthening Community action in the fields of energy, industrial structures and employment.

4. It is not for the working party to comment on the political factors referred to above. But under its general terms of reference concerning the evolution of own resources it can legitimately try by its comments to place the problem of financing the Community in a more accurate perspective than that generally adopted by the Council or the Commission.

5. These comments are as follows:

(a) at their present level, the resources allocated to the Community are still quite marginal in relation to the budgets and total public expenditure of the Member States;

(b) much Community expenditure arises out of a transfer of responsibilities from the Member States to the Community and therefore does not involve any net increase in total public expenditure;

(c) compared with national expenditure, Community expenditure has an appreciable productive effect (multiplier effect and economies of scale);

(d) the effectiveness of certain forms of Community expenditure could be improved, making savings of resources possible;

(e) if its benefits are to be at all significant, Community expenditure must pass a critical threshold, which is still a long way off, and form part of a coherent overall economic policy.

Each of these comments is developed separately in the following paragraphs.

I. THE MARGINAL CHARACTER OF COMMUNITY RESOURCES

6. The overall level of Community resources (14,600 m EUA in 1979) must always be considered in relation to the total amounts raised by the Member States to finance their public expenditure and also in relation to the overall wealth of the Community as expressed by its gross domestic product.

7. The following table demonstrates the very modest size of the Community budget in relation to the total of public expenditure by the Member States in the various sectors in which they are active.

EEC BUDGET AS A PERCENTAGE OF:				
		Member States' budgets	Member States' total public expenditure[1]	Member States' gross domestic product[2]
1973	UA	2.0	1.29	0.53
1974	UA	1.8	1.21	0.51
1975	UA	1.8	1.17	0.55
1976	UA	2.0	1.34	0.61
1977	UA	1.9	1.26	0.57
1978	EUA	2.6	1.71	0.80
1979	EUA	2.8	1.76	0.83

1 Expenditure at Government, regional and local and for social security

2 Nominal value

8. It is also instructive to compare the past rates of growth of these various factors in order to assess the evolution since 1973 of Community expenditure against national expenditure and also against GDP.

9. The following table provides this comparison:

ANNUAL RATE OF GROWTH SINCE 1973					
		EEC Budget	Member States' budgets	Member States' total public expenditure[1]	Member States' gross domestic product[2]
1974	UA	8.5	21.3	16.8	13.5
1975	UA	23.4	27.3	27.1	14.6
1976	UA	28.6	13.2	14.2	16.1
1977	UA	6.1	12.6	13.3	12.8
1978	EUA	45.4	15.6	12.8	10.5
1979	EUA	16.9	11	13.1	12.2

1 Expenditure at government, regional and local and for social security

2 Nominal value

10. Despite their relatively small size, the levying of Community resources can have an unsettling effect on the national budgets of the Member States. The Council's unwillingness to increase Community expenditure is known to be motivated to some extent by a fear of aggravating national budgetary deficits.

Are these fears founded? First of all, it must be pointed out that since 1975 Community resources have not come out of the budgetary revenue of the Member States. They are the Community's own resources collected independently and directly from taxpayers. Moreover, these Community 'own resources' (i.e. levies and customs duties) are payable to the Community by virtue of the existence of a customs union which implies the pooling of such resources. Therefore, any unsettling effect which Community 'levies' may have on national budgets must be considered in the light of the relationship between the Community's non-commercial own resources[1] and the total of the national budgets.

11. The following table illustrates this relationship. Like the preceding tables, it is based on the Community average without reference to the particular budgetary situation of individual Member States. It shows clearly that on average the VAT financial contribution to own resources remains wholly marginal in relation to the overall size of the national budgets and therefore can have no more than a tiny effect on the net budgetary situation of the Member States.

	Non-commercial own resources as a percentage of national budgets[1]	
1975	0.61	UA
1976	0.62	UA
1977	0.56	UA
1978	1.13	EUA
1979	1.35	EUA

[1] GNP and Community VAT contributions

II. THE TRANSFER OF NATIONAL FINANCIAL RESPONSIBILITIES TO THE COMMUNITY

12. It must also be made clear that the financial responsibilities assumed by the Community are not necessarily additional to the existing public expenditure of the Member States.

13. Most of the resources allocated to the Community go to finance expenditure no longer covered by the national budgets: the overall burden on the taxpayer is only slightly increased by this transfer.

---

[1] i.e. from 1975 to 1978 financial contributionswere based on GNP; from 1979 onwards these contributions have been replaced (for six of the Member States) by Community VAT.

14. Over 60% of the Community's resources are devoted to agricultural market support which at present is wholly financed by the Community. Here, the 'transfer effect' is complete, in contrast to policies to improve agricultural structures, which are still largely financed by the States.

15. There are other sectors, such as research and aid (financial and food aid) to developing countries, where at least a partial transfer, of budgetary responsibility has occurred. The exact size of such transfers is, however, difficult to measure in the absence of suitable statistical tools. Furthermore, these transfers are frequently hindered or held up because of opposition from the national administrations which may give rise to an unwarranted increase in the overall financial burden, at least temporarily.

16. However, there are also important areas of Community activity where the overall financial requirement is such that the Community's efforts are added to, rather than substituted for, the efforts of the Member States. Among these areas mention might be made of regional policy as a whole and aid to industrial sectors in difficulty (iron and steel industry).

III. THE PRODUCTIVE EFFECT OF COMMUNITY EXPENDITURE

17. We should recall here a self-evident truth of economics which many people seem to have forgotten, namely that Community expenditure should generally be more productive than the national expenditure which it replaces or supplements.

18. Some Community expenditure has an appreciable multiplier effect, which means that its potential benefit (in economic and budgetary terms) is disproportionately large compared with the outlay. This is particularly true of the creation and organization of the internal Community market. The expenditure incurred (essentially operating expenditure) has opened up a vast unified market which was one of the driving forces behind the economic growth of the 1960s. Similarly, all measures for the harmonization of regulations, manufacturing standards etc. are bound to produce collective benefits far beyond their cost, which is no more than administrative.

19. The same multiplier effect can be found in the EMS where the system's negligible running costs are more than offset by its stabilizing effects and by the resultant savings in terms of intervention by national banks on the foreign exchange markets. Generally speaking, all expenditure on coordination and harmonization has a very considerable multiplier effect.

20. In the field of intervention expenditure, Community action can also be more productive than national measures thanks to economies of scale. Joint action by the Member States permits bigger projects which are more effective than piecemeal action, on a smaller scale, by individual Member States.

In the strict Community context, there have not yet been many examples of joint actions of this type, apart from research and, to a certain extent, data processing. At the level of intergovernmental cooperation, however, a number of joint operations have been launched (particularly in the aerospace field) with the object of cutting project costs.

IV. IMPROVING THE EFFECTIVENESS OF COMMUNITY EXPENDITURE

21. There can be no doubt that the return on Community expenditure, and on public expenditure in general, could be improved. In other words, there is scope for savings in expenditure (and hence resources).

22. The most significant savings could be made in the EAGGF and without having to change the aims and methods of the common agricultural policy. It is clear that in agriculture, only marginal importance has hitherto been attached to costs and financial effectiveness. Greater budgetary discipline both in the planning and the management of the agricultural policy would permit substantial cost reductions.

23. In general, and without wishing to enter into the question of the control of expenditure in the strict sense, since it is outside the scope of the present report, it can be said that the Communities have neither philosophy nor method on cost effectiveness control. Although the financial consequences of new projects are more or less closely scrutinized before adoption, there is no method for calling into question the cost of policies already decided upon and implemented.

The budgetary authority is not concerned with the financial effectiveness of the 'operations voted', i.e. current programmes, and concentrates its attention on the development of those programmes and on new programmes, although they only constitute 10% of the total volume.

24. Your rapporteur therefore considers that a mechanism should be set up for systematically verifying the effectiveness of expenditure in the various areas of Community activity. He believes that two techniques already tried and tested abroad[1] could be usefully applied to Community expenditure:

- systematic review (after two or three years) of all Community expenditure programmes in order to determine whether, having regard to their financial effectiveness, they should be:
  - . cancelled
  - . continued unchanged
  - . continued at a different (higher/lower) level of expenditure
- annual authorization of each programme based on a cost/benefit analysis of all the elements of the programme and in accordance with clear priorities worked out by the Commission.

25. Like most public bodies, the Community does not always pay enough attention to the sound financial management of its policies. It does, however, have the advantage of being a relatively flexible and youthful organization and so should find it easier than the Member States' administrations to stamp out any budgetary laxity by adopting attitudes and methods more conducive to sound financial management.

V. THE 'CRITICAL THRESHOLD' OF COMMUNITY EXPENDITURE

26. It is recognized that in public finance, intervention only achieves its optimum effectiveness above a certain level of expenditure, which obviously varies according to the objective aimed at.

27. Public expenditure programmes only really start to take off where financial intervention reaches a given level in relation to the total cost of the operation. Beyond this critical threshold, the marginal efficiency of expenditure increases considerably, as does the likelihood of actually solving the problem under consideration.

28. However, if expenditure remains below this critical level, it can do no more than prevent the deterioration of a given situation, and funds are likely to be dissipated indefinitely.

---

[1] Particularly the 'Sunset bill' and 'zero-budgeting' systems used in the United States.

29. This principle certainly applies to Community public finance. By way of example two areas can be quoted in which, through lack of sufficient appropriations, intervention did not reach this critical threshold and so failed to achieve its object. Those are, the transformation of agricultural structures (particularly in the dairy sector) and regional disparities.

In essential sectors, such as energy and transport, projects and so expenditure are still only at an embryonic stage and are therefore even further away from this threshold.

30. On a more general level, a group of experts[1] has estimated, on the basis of certain assumptions as to the development of the Community, that the critical threshold for the Community budget might be around 2.5% of the Community's gross domestic product (as against 0.83% in 1979).

Moreover, these experts have been able to calculate that an increase in Community expenditure of some 10,000 mEUA concentrated on the weaker Member States and regions would permit the present per capita income gap between the Member States to be reduced by about 10%.

CONCLUSIONS

31. The working party could set forth a number of findings based on the present document which would provide a general framework for the working party's other more technical proposals. These findings, referred to in paragraph 5 above, can be summarized as follows:

1. Community expenditure represents only a tiny fraction of total public expenditure in the Community and its evolution therefore has no appreciable effect on the internal financial situation of the Member States;

2. Essentially, the financial responsibilities assumed by the Community are in substitution for budgetary responsibilities of the Member States; probably less than 20% of Community expenditure is genuinely additional to national expenditure;

3. Certain types of Community expenditure (particularly in the field of harmonization and coordination of national policies) are especially productive; as far as intervention expenditure is concerned, the Community can finance joint industrial projects more cheaply;

4. The Community's financial management suffers from a lack of budgetary discipline in the planning of certain common policies (in particular, the agricultural guarantee policy) and from the absence of accurate cost/benefit control methods; the competent bodies of Parliament should take specific action in this connection;

[1] Led by Sir Donald McDougall

5. Community expenditure will probably not be fully effective, i.e. profitable, unless it exceeds a threshold which can be estimated roughly at 2.5% of the Community's total gross domestic product, on the assumption that this increase is brought about principally by the transfer of the public responsibilities of the Member States to the Community, and therefore without any significant increase in the overall tax burden on the individual.

Only if the budget passes this threshold will it be possible to have effective management at Community level of those projects which cannot be undertaken individually by the Member States and whose development requires coordination and cooperation between the Member States.

II.

an assessment of the present system of
own resources for the Communities

Draftsman: Mr ANSQUER

INTRODUCTION

1. This document is based on the guidelines set out in the chapter of the working party's programme of work entitled 'analysis of and changes to existing own resources'.

2. With the Commission's assistance the working party has reviewed and analysed in depth all the sources of Community revenue, concentrating particularly on the three main ones:

- agricultural levies,
- customs duties,
- VAT.

3. This document simply sets out to explain the main problems created by the present system of resources and to put forward in as much detail as possible suggestions for improvements.

4. After a brief statistical statement of the volume of the various resources, the document goes on to discuss the following points:

(1) specific problems relating to different types of resources;
(2) the financial independence of the Community;
(3) inspection measures for the collection of resources.

Two further chapters are devoted to specific problems raised by para-fiscal and ECSC resources.

I. THE VOLUME, TREND AND BREAKDOWN OF OWN RESOURCES

(a) Present situation

5. The most recent figures available on Community resources relate to the 1979 financial year[1]; they can be readily compared with those in the new preliminary draft budget for 1980 (presented by the Commission on 19 February 1980):

---

[1] Figures based on actual results.

	m.EUA 1979	1980
Agricultural levies.................	1,679	1,686
Sugar/isoglucose levies.............	465	491
Customs duties......................	5,189	5,668
VAT[1].............................	4,738	6,694
GNP contributions[2].................	2,302	-
Other...............................	231	173
TOTAL............	14,604	14,712

[1]paid by six Member States in 1979 and nine in 1980

[2]paid by three Member States in 1979.

(b) Breakdown of the various own resources

The trend since 1975 is set out below:

	Levies	Customs duties	GNP contributions VAT resources (+ miscellaneous revenue)
1975............	9.5	50.7	39.8[2]
1976............	14.5	50.8	34.7[2]
1977............	21	46.3	32.7[2]
1978............	18.8	36	46.2[2]
1979............	14.7	35.5	49.8[3]
1980[1]..........	14.8	38.5	46.7[4]

[1] new preliminary draft budget of 29.2.1980

[2] Gross National Product contributions

[3] GNP contributions for three Member States and VAT for six Member States

[4] VAT for nine Member States

(c) Trend in the rate and yield of VAT

In 1979 the VAT rate was......................................0.79%

for 1980:

- the rate proposed in the initial preliminary draft budget (including letters of amendment Nos. 1 and 2) 0.89%
- the rate proposed in the draft budget (of 23 November) was..0.77%
- the rate proposed in the new preliminary draft budget of the Commission is...............................0.68%

6. According to the Commission's latest forecasts the maximum yield from Community VAT - i.e. from the 1% rate - for the period 1980/1983 would be:

	m.EUA
1980	9,900
1981	10,900
1982	11,900
1983	(12,900 (13,900

(d) Total own resources available for the period 1980/1983

7. On the basis of the Commission's latest forecasts the total volume of own resources available in 1980/1983 under the present system would be:

m.EUA

	Levies and sugar levies	Customs duties	1% VAT	Total
1980	2,177	5,668	9,910	17,755
1981	2,183	6,037	10,910	19,130
1982	2,243	6,488	11,924	20,655
1983	2,288	6,942	13,235	22,465

8. It is clear that these forecasts are very unreliable given:

- the very unstable natur of world/Community agricultural prices and hence of the levies;
- the uncertainties surrounding future trade flows and hence the revenue accruing from customs duties;
- the uncertainty about the yield of the VAT assessment basis in the absence of final results for the first financial year in which this new resource was fully applied (1979).

9. Overall, the Commission's estimates would suggest the following average annual growth rates for each of the three main categories of own resources:

- levies.......................... + 1 to + 2%
- customs duties.................. + 6 to + 7%
- VAT............................. + 10 to + 11%.

II. PROBLEMS RELATING TO THE VARIOUS TYPES OF RESOURCES

10. By separating trade-linked own resources (levies and customs duties) from Community VAT, it is possible to attempt to list the main advantages and disadvantages of these resources.

(a) Trade-linked own resources

11. On the positive side these resources are <u>genuine</u> Community resources in that they are:

. paid in full, directly and automatically to the Community,

. linked to the operation of various common policies which constitute the very foundations of the Community: agricultural policy, commercial policy and Community preference.

12. These resources do however present a number of political and financial drawbacks:

. they are indirect taxes of which European taxpayers are totally unaware and hence do nothing to reinforce Community solidarity;

. they fluctuate quite independently of budgetary financing requirements;

. they are not dynamic: the extension of Community preference and the general reduction in customs duties mean that they actually grow more slowly than budgetary needs or even inflation;

. 10% of the yield is paid back to the Member States by way of reimbursement of the collection costs incurred by national customs services; in 1979 some 733 million EUA was repaid in this way.

(b) <u>VAT</u>

13. The initial results of the application (to six Member States) of VAT in the period since 1 January 1979 will not be known until July 1980 and only then will it be possible to make an initial assessment of the operation of this new resource.

14. However, a number of points can be made at this stage, namely:

- VAT is not a specifically Community tax; admittedly the Community rate is applied directly to the harmonized basis of assessment quite independently of the various national rates: it does not therefore represent a surtax on national VAT nor a levy on the national VAT yield. This tax is however an indirect tax <u>shared</u> between the Community and the Member States - and taxpayers are aware for the most part of the national component, which accounts for a far greater proportion;

- VAT is a more suitable way of financing the budget than trade-linked own resources as its rate is a direct function of expenditure requirements, being calculated on the basis of the difference between total approved expenditure and the total revenue expected from trade-linked resources;

- VAT is a fairly dynamic tax in that it keeps pace with consumption and inflation; it does not however grow at a faster rate than these two parameters unlike direct taxes;

- a number of problems relating to the assessment basis and the collection of Community VAT have still to be solved. Although harmonized, the VAT assessment basis in the nine Member States is still subject to many exceptions, derogations and exemptions which could be abolished from 1 January 1983. Moreover, VAT is collected essentially on the basis of statistical estimates and not the declarations submitted by those subject to the tax; the regulation implementing the sixth VAT directive leaves the Member States free to choose between these two methods and eight of them have chosen the former, which eliminates any visible link between the taxpayer and the Community as it is the national revenue services which calculate the Community and national share of the VAT yield; this aspect is also due to be standardized in 1983.

(c) Proposals of the working party

15. Despite their inadequacies and imperfections these two types of own resources are a great achievement of the Community and one which must be preserved. The working party might therefore confine itself to requesting that the following improvements be made to the existing system of Community VAT by 1 January 1983:

- harmonization of the entire basis of assessment;

- wider use of the declaration-based method of collection.

III. THE FINANCIAL INDEPENDENCE OF THE COMMUNITY

16. The existence of Community own resources is not in itself sufficient to guarantee the Community total financial independence from the Member States. Before this can happen the Commission must be able to calculate these resources independently, it must be free to dispose of them as it wishes and they must no longer be included in national budgets.

(a) Estimating own resources

17. When preparing the draft budget it is necessary to estimate the resources likely to be available for the following financial year: this estimate is very important as it may have a direct bearing on the volume of expenditure authorized; we all know for example how the prospect - based on revenue estimates - of exceeding the 1% VAT ceiling can induce one or other of the parties composing the budget authority to restrict the level of appropriations authorized.

18. It is essential therefore that the Commission should have the right and the means to prepare completely independent estimates of resources. The situation seems reasonably satisfactory in this respect as the Commission makes its own forecasts, compares them with those of the Member States in the context of the Advisory Committee on the Community's Own Resources and then adopts the final estimates quite independently.

19. It remains to be seen to what extent the Commission possesses the means to verify the accuracy of the data (provided by the Member States) on which its own forecasts are based: the problem of inspection is considered later.

(b) Making own resources available to the Commission

20. The own resources indentified by the Member States are credited to the Commission's account with the national treasuries on the basis of the sums actually collected, in the case of customs duties and levies, and by monthly twelfths (twelfths of the total annual forecast) in the case of VAT.

21. Article 12 of the regulation implementing the system of own resources[1] states that:

> 'The Commission shall draw on the sums credited to the accounts referred to in Article 9(1) to the extent necessary to cover its cash resource requirements arising out of the implementation of the budget'.

22. In its present form the text is capable of guarnateeing a measure of genuine financial autonomy for the Commission (and by extension the Community) in the form of an automatic drawing right - provided the reference to 'cash resource requirements' does not require the Commission to justify its withdrawals nor authorize the Member States to check that they have been made in a proper manner (this inspection function being the exclusive preserve of the European Court of Auditors).

---

[1] Regulation No. 2891/77 of 19.12.1977 - OJ L 336, p.1, 27.12.1977

(c) Exclusion of own resources from national budgets

23. Clearly own resources should no longer be shown in the national budgets, as Community legislation (namely the decision of 21 April 1980) authorizes the principle of direct collection of such resources by the Community and the Community budget lays down the annual amount.

24. To include Community resources in national budgets would be not only illegal but dangerous as these resources might then become dependent on the fate of national finance. The situation in the various Member States is not very clear in this respect; some seem to persist in showing different types of own resources in some form or another in their national budgets with the result that these resources are subject to formal approval by the national parliaments.

25. The Commission should carry out a detailed study of the situation and, where necessary, ask Member States to fall into line, on the understanding that national parliaments may still and indeed should be kept duly informed of the amount of revenue allocated each year to the Community.

IV. INSPECTION MEASURES FOR THE COLLECTION OF OWN RESOURCES

26. It is in the Community's own best interests to have available reliable own resources i.e. resources which have been accurately checked. As matters stand at present the inspection measures do not appear satisfactory as it would seem that resources are not always properly collected and Community powers of inspection would appear to be too limited.

27. The working party could therefore propose a number of measures to improve the situation:

(a) Proper collection of resources

28. Although the Commission undoubtedly receives all the own resources collected by the Member States, there is no certainty that the latter actually collect all the sums they should.

29. There is clearly a risk that the relevant national administrations will show less vigour in collecting trade-linked own resources as these resources are paid wholly to the Community. This lack of vigour can lead not only to a loss of Community resources but also allow fraudulent practices (e.g. on refunds) to take place on a large scale, which are both expensive and adversely affect the Community's image.

30. No such lack of vigour is evident in the case of VAT as the major share of the revenue yielded by this tax goes to the Member States.

They are, however, great differences in the effectiveness of the inspection machinery in the various Member States and it is known that in some VAT fraud may account for 20 to 30% of the national tax yield. This is a serious situation as it may lead to a definite imbalance in the contributions of the various Member States, making some reluctant to agree to increase the Community rate of VAT or even to oppose the very principle of the tax.

(b) Community powers of inspection

31. Pursuant to the existing legal texts (particularly the regulation implementing the system of own resources referred to above), responsibility for ensuring that these resources are properly collected mainly falls to the Member States.

The Commission may, however, ask for additional inspection measures, in which it may be involved, and can also request that certain documents be forwarded to it.

32. The Court of Auditors has much wider powers but exercises these in conjunction with national inspectorates and as part of a posteriori verification procedures.

33. All in all therefore the Commission is not able to carry out rapid and widespread checks on the collection of own resources.

(c) Working party proposals

34. The Commission's powers of independent inspection over levies and customs duties must be strengthened by providing it with the legal and material means to establish permanent inspectorates on the territory of the Member States which would have the same powers of investigation in respect of documents and premises as those of national inspectorates. These inspection measures would concentrate on the supervision of revenue collection and could be carried out by a small number of senior staff.

35. The problem of VAT is less straightforward as this is essentially a national tax and inspection takes place at the level of the taxpayers. Efforts should therefore be concentrated on harmonizing national collection and inspection rules - on the basis of Commission proposals modelled on the most advanced national systems. National rules on collection and inspection of trade-linked own resources should also be harmonized.

V. PARA-FISCAL RESOURCES

36. In addition to the traditional type of own resources considered so far, the working party should also look at the problems raised by the recent development of what may be called para-fiscal Community resources.

(a) What is meant by para-fiscal taxes?

37. This term is generally applied to all those taxes which fall outside the general budgetary rules. Para-fiscal taxes may be characterized as follows:

- the decision in principle, to introduce these taxes, the rate of tax and the use to which the revenue accruing there from is put are not subject to parliamentary approval in the same way as ordinary taxes, but are decided by the executive alone;

- the yield from these taxes is earmarked for specific items of expenditure and not lumped together with other resources as the principle of budgetary universality and non-allocation of revenue would require;

- these taxes are entered in the budget in a separate and different manner from normal revenue and expenditure.

38. The grounds involved for the introduction of para-fiscal taxes are usually those of flexibility and convenience. They are claimed to suit particular types of economic or financial situations which cannot be solved by normal budgetary means. Several Member States have introduced para-fiscal taxes to varying degrees.

39. From Parliament's point of view these taxes raise a major problem as they represent a serious violation of the principle whereby the collection of revenue and the implementation of expenditure require democratic authorization; the exceptional budgetary status of these taxes often denies Parliament any real monitoring powers.

(b) Community para-fiscal taxes: the co-responsibility levy on milk

40. In the Community context there is at present only one para-fiscal tax, the co-responsibility levy on milk production.

Operation of the co-responsibility levy

41. This levy was introduced in 1977 by a Council regulation[1] which provides for the rate of the levy and implementing arrangements to be adopted annually in the form of a regulation as part of the annual agricultural price review. The legal basis for the regulation which covers

[1] Regulation of 17.5.1977 - OJ L 131, 26.5.1977, P.6.

only milk production is Article 40(3) of the EEC Treaty[1]. In principle the yield from this tax is allocated to meet expenditure of a specific nature intended to promote the development of outlets for milk products. These 'resources' are entered - as negative expenditure - in the chapter of the budget devoted to expenditure in the milk sector. Their utilization is recorded in separate accounts governed by special rules.

<u>The legal position</u>

42. The legal status of this levy is not very clear. A judgement handed down by the Court of Justice on 21 February 1979 confirmed that the tax was legal in principle on the basis of Article 40 of the EEC Treaty and that taxes of this type could be introduced in the context of the common organization of markets without recourse to the procedure laid down for the creation of new resources (Article 201 of the EEC Treaty). The Court did not give a ruling on the problem of the budgetization of this levy, nor a fortiori on its democratic legitimacy.

The Court of Auditors in its report on the budget for the 1978 financial year criticized the inclusion of this tax in the budget as a negative item of expenditure, the utilization of which was not subject to any of the rules laid down in the Financial Regulation.

<u>The growing problem of the co-responsibility levy</u>

43. This levy, which was originally introduced for a three-year period, now seems to have acquired a permanent status and has become one of the main factors in the policy of balancing Community expenditure in the milk sector. In addition, the levy, which originally produced a small yield, now brings in some 500 million EUA[2]. The possibility is now being discussed of extending the concept of a special levy on production to other agricultural sectors (particularly production of alcohol), or even to non-agricultural products (e.g. Community levy on oil).

---

[1] <u>Article 40(3) of the EEC Treaty</u>
'The common organization established in accordance with paragraph 2 may include all measures required to attain the objectives set out in in Article 39, in particular regulation of prices, aids for the production and marketing of the various products, storage and carry over arrangements and common machinery for stabilizing imports imports or exports'

[2] Equivalent to a rate of 1.5% (see the Commission's proposals for the 1980/81 marketing year).

(c) Working Party proposals

44. Faced with this situation and with a view to limiting the erosion of the European Parliament's powers by this type of 'taxation without representation', the working party could propose the following remedies:

(1) restriction of para-fiscal taxes to agriculture;
(2) introduction of such taxes and establishment of their annual rate by means of 'legislative conciliation' between Parliament and the Council;
(3) budgetization - in an annex to the general budget - of revenue and expenditure relating to such taxes;
(4) approval by the budgetary authority in accordance with the standard procedure of the various forms of expenditure to which the revenue accruing from such taxes is applied.

VI. FINANCIAL RESOURCES OF THE ECSC

45. As part of its assessment of the present system of Community own resources the working party should examine the problems raised by the present state of depletion of ECSC financial resources and put forward its proposals for remedying the situation.

(a) Depletion of ECSC financial resources

46. The serious financial crisis to which the Community's coal and steel industry has been exposed since 1970 has highlighted the inadequacy of the financial resources available to the ECSC to cope with the crisis.

47. The main source of ECSC revenue is of course the levy on the production of coal and steel up to the 1% ceiling on the agreed assessment basis.

48. Because of the financial crisis facing those companies which are subject to the levy, the rate has remained fixed at 0.29% since the beginning of 1970[1] - equivalent to a yield of about 100 million EUA - and the ECSC has therefore been unable to obtain adequate funds to provide effective assistance to these undertakings, notably by carrying out the modernization, conversion and readaptation measures provided for in the ECSC Treaty.

49. While the ECSC has been able by borrowing and lending operations to make a positive contribution to the efforts of individual undertakings

[1] Rate increased to 0.31% in 1980

and the Member States, even here the lack of resources raised from taxation has restricted its contribution, in particular by reducing the level of interest rate relief available on certain types of loans.

(b) Possible solutions

50. The Commission has tried, albeit rather late, in the day, to come up with solutions to the financial crisis.

51. In May 1978 it proposed that the Member States should allocate to the ECSC the yield from customs duties on imported coal and steel products. Paradoxically, these duties - estimated to be worth some 60 Million EUA a year - accrue to the Member States, whereas all other customs duties are of course paid to the Community. The Council did not act on this proposal for a variety of reasons one of which was the very unequal distribution of duties among the Member States (one Member State accounted for almost 50% of the total).

52. More recently, in May 1979, the Commission proposed allocating to the ECSC a total of 100 million EUA to finance special temporary allowances for workers in the steel industry. This amount would have been credited first to the EEC budget and then transferred to the ECSC budget. Once again the Council did not act on the proposal, which in any case would not have solved the general problem of financing the ECSC but would merely have increased its resources for the provision of social aid.

53. Under these circumstances the Commission has been forced to resort to a temporary expedient. It requested and obtained the approval of the 'representatives of the governments meeting in the Council' for national contributions in the form of donations to the ECSC. In the 1978/79 financial years these contributions paid by Member States according to an ad hoc scale totalled 28 million EUA. There is no need to emphasise the inadequacy of and lack of Community spirit implicit in such donations.

(c) The solution advocated by Parliament

54. Parliament was quick to consider the financial problems facing the ECSC and rapidly reached the conclusion that the only lasting solution to the structural financial crisis facing the ECSC was to bring the EEC and ECSC budgets closer together or to be more precise to vote an annual subsidy in the context of the EEC budget which would then be transferred to the ECSC budget[1].

55. After much hesitation, mainly on legal grounds, the Commission took up this proposal in the framework of the ECSC budget for 1980 but felt that a Council regulation based on Article 235 EEC was necessary before the transfer could be effected; it also asked the budgetary authority to give its opinion

[1] Reports of the European Parliament on the ECSC budgets for 1977/1978/1979 and the report of the European Parliament on certain budgetary questions (Doc.150/78)

as soon as possible on the principles of such a transfer.

(d) Working party proposals

56. In the light of the above considerations, the working party could put forward the following proposals to remedy the financing problems facing the ECSC:

(1) the proposal to make available to the ECSC the revenue accruing from customs duties on imports of coal and steel products is wholly justified. The Council must give this proposal serious consideration in the framework of a conciliation procedure with Parliament, which the latter should take steps to initiate as soon as possible;

(2) the proposal to transfer to the ECSC on annual subsidy from the EEC budget is entirely justified. The level of the subsidy must be decided by the budget and authority in the framework of the budget procedure and on the basis of the ECSC's residual financing requirements. The High Authority must be free to decide how the subsidy should be spent. The decision on the principle of such a transfer may be taken by the budgetary authority without recourse to the procedure provided for in Article 235 of the EEC Treaty.

CONCLUSIONS

57. The working party might put forward the following proposals on the basis of the above study of various aspects of the present system of Community own resources:

(1) technical improvement of existing machinery

- by harmonizing the entire basis of assessment for VAT and extending to all Member States the declaration-based collection method by 1 January 1983.

(2) strengthening of the Community's financial independence

- by guaranteeing the Commission's freedom to prepare forecasts and the handing over of own resources,
- by refraining from entering Community own resources in national finance acts.

(3) strengthening Community inspection powers in respect of the collection of own resources

- by harmonizing national rules on collection and inspection procedures in the context of trade-linked resources (levies/customs duties) and VAT,
- by granting the Commission the right and the means to exercise direct permanent powers of inspection over the collection of trade-linked resources.

(4) Controlling the development of Community para-fiscal taxes

- by strictly limiting para-fiscal taxes to the agricultural sector,
- by following the conciliation procedure when introducing and fixing the rate of such taxes,
- by entering these taxes in a separate and detailed manner in the budget and making them wholly subject to normal budgetary approval procedures.

(5) strengthening ECSC finances

- by allocating to the ECSC the revenue accruing from customs duties on coal and steel products; Parliament must take steps to initiate a conciliation procedure with the Council on this question,
- by transferring to the ECSC a subsidy from the EEC budget to be determined annually by the Budgetary Authority in the light of actual requirements.

-:-:-:-

III.

the Community's loan policy

Draftsman: Mr J.M. TAYLOR

INTRODUCTION

1. This document develops the ideas contained in the section of the working party's work programme relating to loan policy.

2. The principal idea is that loans should be considered as a unique kind of own resource. Instead of relying entirely on revenue provided by the taxpayer the Community can catalyse certain types of desirable activity with money borrowed on the capital markets and then lent to public and private sectors. That is making things happen that would not otherwise happen. ("However these loan financing operations .... are not to be confused with budgetary expenditure. The latter may supply, however, interest-rate subsidies on the former": MacDougall Report).

3. Indeed, the Community has from the outset been involved in the various financial activities provided for explicitly in the ECSC and Euratom Treaties and implicitly in the EEC Treaty.

4. The purpose of this report is to examine to what extent, and in what way, greater use could be made of loans to finance certain types of Community action.

5. After a brief description of the present situation, the report will:

- re-state the European Parliament's attitude to Community loans,
- show that this sector should and can be developed,
- put forward practical proposals for this purpose.

o

o o

I. COMMUNITY LOAN MECHANISMS

6. There are at present five separate loan mechanisms:

- ECSC loans for investment in the coal and iron and steel industries;
- Euratom loans for the production of nuclear electricity,
- Community loans (EEC) for Member States with balance of payments difficulties resulting from the oil-price increases,
- investment loans (EEC) to promote investment within the Community (also referred to as NCI loans),
- EIB loans for regional development, the promotion of undertakings and projects involving several Member States.

7. A schematic table of these mechanisms is annexed to this report.

8. The table shows that:

- the Community borrows a substantial amount each year;

Financial year 1979	(m EUA)
ECSC	957
Euratom	165
Community loans (1977)	1,816
Investment loans (NIC)	177
EIB	2,480
Total	5,595

Budgetary own resources for the 1979 financial year totalled 14,584 m EUA. Resource available from borrowing was therefore equivalent to around 38% of the Community's tax revenue;

- the structure and management of the existing loan mechanisms vary widely since they were set up and have developed quite independently;

- all the money borrowed is used to finance loans and not non-refundable subsidies. Leaving aside interest rate subsidies and financial expenses, loans raised by the Community are therefore neutral transactions involving no actual expenditure by the Community, which simply acts as an intermediary.

o

o o

II. PARLIAMENT'S ATTITUDE TO LOAN POLICY

9. Since 1975, when Euratom loans were introduced, Parliament has followed closely the development of the various borrowing/lending mechanisms and has thus gradually established a firm position on loan policy[1].

10. In general, Parliament is in favour of borrowing to obtain resources to finance certain types of Community action. It feels that:

- by borrowing it is possible to obtain substantial resources needed to finance investment projects capable of reducing the disparity between the levels of development of the various Community regions;

---

1 See in particular the latest report (1978) on the inter-institutional dialogue on certain budgetary questions (Doc. 150/78)

- borrowing is a flexible method of financing, particularly well adapted to financing the productive activities which the Community will be increasingly called upon to undertake; especially in problem sectors where a Community-level solution is needed;
- recourse to borrowing is in line with the principle of the Community's financial independence.

11. Parliament nevertheless considers that greater recourse to borrowing must be subject to two conditions: Community loan policy must be both rationalized and controlled. These two aspects are briefly discussed below.

1. Rationalization of the loan policy

12. Reference has already been made to the diversity of the existing mechanisms. This has several drawbacks:

- the lack of an overall picture of the Community's need for funds and its capacity to borrow; this prevents the formation of a genuine loan policy and gives rise to uncertainty about the position of loans in relation to tax revenue;

- dispersal of responsibility for decision-making and management between various departments and institutions;

- an uncoordinated approach to the major capital market which is likely to create confusion harmful to the Community's international credit standing.

13. Parliament recommended some degree of unification of the mechanisms which are the responsibility of the Community institutions proper and more systematic coordination between this unified mechanism and the EIB's operations.

14. This solution obviously raises a number of problems connected with the existence of separate Treaties and regulations, which perhaps explains the Commission's lack of enthusiasm with regard to Parliament's proposed rationalization.

15. Parliament is nevertheless convinced that, in view of the lack of coordination between the mechanisms, it is impossible either to make maximum use of or to develop borrowing/lending operations. It should therefore again request the Commission to review the existing system and to formulate a genuine loan policy based on new principles.

2. Control of the loan policy

16. If this policy is to be developed, it must remain subject to adequate political and budgetary control.

Political control

17. Parliament has in the past made quite clear the way in which loan policy should be controlled by the various institutions. The system it has proposed is as follows:

- on a proposal from the Commission and after conciliation with Parliament, the Council decides to raise a loan to finance a particular measure; it also decides the general framework for the loan operations;
- subject to a ceiling which it fixes annually, the budgetary authority authorizes recourse to borrowing and lending (see below);
- the Commission assumes full responsibility for management, that is, it decides on individual borrowing and lending operations within the annual budgetary allocation;
- in addition to its own activities as defined in Article 130 of the EEC Treaty, the EIB assists the Commission in its task of management without infringing on the latter's initiative and responsibility.

Budgetary control

18. Since 1976 Parliament has insisted that the Community's borrowing/lending operations (with the exception of the EIB's activities) should be entered in the budget and thus controlled each year by the budgetary authority. It therefore proposed the creation of a capital budget which would form the second part of the general budget of the Communities and whose adoption would be subject to the relevant rules laid down in the Treaties.

19. The capital budget has existed in an embryonic and unsatisfactory form since 1977. The Council and Parliament are currently considering ways of improving it as part of the conciliation procedure relating to the revision of the Financial Regulation. It is therefore sufficient to point out that the budgetization of loans should enable the budgetary authority:

- to authorize borrowing/lending operations each year on the basis of the rules in force and of actual requirements;
- to be kept informed during the year of the implementation of these operations;
- to verify in retrospect, during the discharge procedure, that the operations have been managed in a sound and proper manner.

20. Parliament takes the view that the development of loan policy must be subject to this dual control (political and budgetary) in view of the volume of operations financed in this way, the nature of the measures involved (energy, economic infrastructures, regional development, etc.), the resulting Community debt and the fact that repayment is guaranteed by the ordinary budget.

21. Parliament should therefore reiterate its demands to the Commission and the Council to ensure that its proposals in this field are taken into account.

o

o o

III. THE DEVELOPMENT OF LOAN POLICY: NECESSARY AND FEASIBLE

22. Resources obtained through borrowing must complement and not replace revenue from taxes. This principle must be clearly stated at the outset.

23. The majority of the measures at present financed from the own resources of the ordinary budget could not be financed by borrowing, since they involve non-refundable subsidies. It could however provide new resources better suited to financing other measures, the need for which is now being felt.

Necessary

24. For reasons connected with the trend in the process of integration, the general economic situation in the Member States and the widening of the disparity between their levels of development, the Community has been obliged to adopt a new policy designed to promote productive investment and to achieve the convergence of the national economies.

25. This policy covers several sectors, including energy, industry and transport. Since the investment projects in these sectors which are eligible for Community aid have both productive and commercial objectives, it would be unreasonable for the aid to consist solely of subsidies financed from the Community's tax revenue. It would be more appropriate to have recourse to loans financed by borrowing, possibly at reduced interest rates.

26. The forthcoming accession to the Community of countries whose economies are expanding rapidly will increase still further the need for financing obtained through borrowing/lending. In the long-term, this mechanism might also be used to support a counter-cyclical policy designed to attenuate the effects of the economic cycle in the various Member States[1].

Feasible

27. The Community has already gained considerable experience in the financial sector through the existing mechanisms.[2] Moreover, the Community enjoys a good reputation on the international capital markets in respect of its sound management and the quality of its financial guarantees.

28. It is therefore likely that a substantial increase in the Community's loan activities would be well received by the principal international financial markets. There is even a possibility that Community intervention on those markets would be more decisive and more effective than the individual and competitive measures taken by the Member States or national loan bodies (treasuries, banks, public enterprises, etc.), since the Community is in a better position to compete, for example, for petro-dollars, against the major third countries (United States and Japan). In this connection, there is much to be learned from the Community's activities in major international trade negotiations.

o

o o

[1] See in this connection the conclusions of the MacDougal study group: The MacDougal report urges the Community to consider "limited borrowing powers (for relatively short periods) to avoid a pro-cyclical influence from the budget, and to 'lean in the right direction' so far as the general thrust of coordinated national conjunctural policies is concerned ....." But the same report cautions that "It is hard to envisage the adequate debt financing power and mechanisms which a Community anti-cyclical budgetary policy would require, in a framework where control of monetary policy and access to the Member States' capital markets are jealously guarded national prerogatives"

[2] The Memorandum on the Proposed Second NCI tranche COM(80) 20 final has this to say: "Experience with the first tranche has demonstrated the usefulness of the new instrument. The Community's borrowing capacity has added significantly to the incentive to investment in the sectors chosen for priority attention.

IV. PROPOSALS FOR DEVELOPING BORROWING/LENDING POLICY

29. As pointed out above (point 8), money borrowed by the Community in the context of the existing mechanisms is used exclusively to finance loans to private and public bodies in the Member States. The Community takes the initiative and acts as an intermediary between the capital markets and the investors; it also provides security and guarantees and, in exceptional cases, finances the interest rebates granted to certain borrowers.[1]

30. Hence the Community does not use the money it borrows to finance non-refundable subsidies, which are commonly used by the Member States as part of their deficit spending policy.

31. The working party feels that, under present conditions, the Community should limit its financial activities to balanced operations of borrowing and lending - and should not borrow money with a view to financing some items of expenditure or to balancing its accounts. However, this possibility should not be definitively discounted - and could be re-examined at a later stage.

32. On this basis Community borrowing/lending policy could develop along the following broad lines:

Total volume

33. Taking account of the Community's requirements and the funds available to it and of the situation on the international financial markets, Community borrowing/lending activities (excluding EIB) should grow rapidly to an average annual volume of around 5,000 million EUA.[2]

[1] EIB and NCI loans to beneficiaries in Italy or Ireland may be subsidized to a maximum of 200 m EUA each year. These subsidies are connected with the introduction of the EMS.

[2] See in Annex 2 more detailed considerations on this point.

34. This figure may at first sight seem high but it represents the minimum which many feel necessary to pursue, at Community level, a new common policy of the kind defined above (points 24 to 26) aimed at promoting investment and reducing the divergence between the national economies.

35. The working party believes that the Community will not encounter any non-political difficulties in obtaining these resources on the financial markets or in selecting projects requiring an equivalent volume of finance.

A broadly-based and voluntarist loan policy

36. The new mechanism should be as broadly based as possible in that it should provide financing for an extremely wide range of investments which are of benefit to the general public (energy, industry, transport, communications, etc.).

37. The mechanism should also be used to finance loans which reflect a specific policy of economic development at Community level. It should not be used to co-finance, or refinance, projects devised unilaterally by the Member States (which may be uncoordinated or even in competition with each other). This development policy should be defined by the Council and Parliament on a proposal from the Commission, which would also be responsible for its implementation.

An adequate financial incentive

38. Although by their very nature Community loans can be used only to finance productive investments, it is highly desirable that the loans should be accompanied by financial advantages which will encourage investors to apply for them.

39. In particular, the loans should, as a general rule , carry interest rebates financed by the Community budget and at a rate varying (for example from 1% to 5%) in accordance with the type of project involved.

40. Investors should automatically be granted reasonable exchange guarantees to be provided by the Community budget.

Extension of the NCI

41. The New Community Instrument (investment loans), set up in 1978, clearly meets to a large extent the conditions outlined above and could therefore form the basis for the recommended development of Community loan policy.

42. However, the working party feels that substantial modifications are required, not only as regards its overall financial volume (the NCI is subject to a ceiling of 1,000 million EUA) but also in the light of the reservations expressed by the European Parliament when the basic regulation was adopted. At that time Parliament requested that:

- the system should be established on a permanent basis,
- the concept of loan tranches opened by Council decision should be eliminated,
- the Commission should retain ultimate responsibility for the loan operations, with the EIB acting merely in a technical and intermediary capacity.

43. The NCI should be accompanied by the financial incentives recommended by the working party (interest rebates and exchange guarantees).

44. The regulation establishing the NCI provides for a review of the system before the end of the 1980 financial year. The ideas put forward above could be taken into consideration on that occasion.

A Proposal: the creation of EC bonds

45. The working party is not required to draft detailed technical proposals but simply to submit suggestions based on a particular political conception of the way in which the Community could use the loan mechanism.

46. The working party feels that the general public should be given greater opportunities of subscribing to Community loans. For example, subject to certain conditions, EC loans could be modelled on the system of government loans used in the Member States.

47. Such EC bonds would thus:

- be to a large extent open to public subscription (through the banks and the various credit organizations) in the form of bonds at a low unit price (for example 100 or 200 EUA)[1],
- issued simultaneously throughout the Community financial market,
- if possible denominated in ECU and hence indexed,
- guaranteed by the Community budget.

48. In addition to the financial advantages of such a mechanism (in particular a reduction in the EC's external debt), it could develop a direct and practical interest among the general public in the construction of Europe and increase the feeling of Community solidarity among its citizens.

o

o o

---

1 Certain types of Community loans (EIB and ECSC) are already open to public subscription but in a very limited form which in practice restricts access to a tiny minority of individual savers.

CONCLUSIONS

49. The following conclusions could be drawn from this document for the purpose of drafting the working party's final report:

1. Confirmation of the favourable opinions expressed by Parliament in the past with regard to the development of loan policy, provided that it is satisfactorily rationalized and controlled;

2. loan policy must be developed to finance policies aimed at promoting productive investment and reducing the divergence between the national economies;

3. such development is feasible in view both of the experience and results already obtained in this sector and of the potential for Community intervention on the international capital markets;

4. as conceived at present, Community borrowing/lending operations should expand considerably to reach an average annual volume of around 5,000 million EUA;

5. this increase should make it possible to finance as wide a range of investments as possible in accordance with a specific Community economic development policy. Financial incentives and guarantees should be offered to investors;

6. the development of loan policy could be based on the existing NCI mechanism, subject to the modifications recommended by Parliament when it was introduced;

7. in view of their financial and political advantages, EC bonds should be offered directly for subscription by private investors.

ANNEX 1

SUMMARY TABLE OF

COMMUNITY BORROWING AND LENDING OPERATIONS

	ECSC LOANS	EURATOM LOANS	COMMUNITY LOANS (EEC)	INVESTMENT LOANS (EEC)	EIB LOANS
1. Legal basis	ECSC Treaty: Arts. 49 & 51 para. 1 Art. 54	Euratom Treaty (Art. 172 para. 4) and Council decision of 29.3.77	EEC Treaty (Art. 235) Council decision of 17.2.75	EEC Treaty (Art. 235) Council decision of 16.10.78	EEC Treaty (Art. 129, 130) + protocol annexed to the Treaty
2. Nature	Financing of programmes for - investments - modernization - reconversion - housing in the coal/steel industry	Financing of investment programmes for the building of nuclear power stations	Financing of loans to Member States in balance of payments difficulties due to the rise in prices of oil products (i.e. recycling of petro. dollars)	Financing of investment programmes in the energy, industry and infrastructure sectors (in view of contributing to greater convergence and integration of national economic policies)	Financing of projects in relation to regional development - modernization, conversion or creation of undertakings called for by the establishment of the EEC - projects of common interest to several Member States The EIB may also make loans in third countries
	Funds obtained by borrowing may not be used except to grant loans	Borrowings are limited to the amount of actual loan requests	Borrowings are limited to the amount of actual loan requests		Loans are based on borrowings and on the EIB own resources
3. Authority responsible for					
- borrowing	EEC Commission (DG XVIII)	EEC Commission (DG XVIII)	Borrowing and lending decisions are taken by the Council on an ad hoc basis.	Council decides the launching of each borrowing/lending tranche	The EIB is directed by the Board of Governors (which consists of Finance Ministers of Member States)
- lending	EEC Commission (DG XVIII)	EEC Commission (DG XVIII) (in coordination with the EIB's own operations in this sector)	The Commission is responsible for conducting the operations	The Commission is responsible for borrowing Loans are examined and granted by the Commission and the EIB	Loans are decided by the Board of Directors, appointed by Governors

	ECSC LOANS	EURATOM LOANS	COMMUNITY LOANS (EEC)	INVESTMENT LOANS (EEC)	EIB LOANS
- <u>management</u>	EEC Commission (DG XVIII)	EIB acts as a trustee for the Commission	The European Fund for Monetary Cooperation is responsible for the transfer of funds	The EIB is responsible for the management of the loans	The Management Committee is appointed by Governors
4. <u>Ceilings</u>	None	Initial ceiling: 500 mUA (Council decision of 29.3.77) New ceiling: 1,000 mUA (Council decision of) (Both decisions were taken without information/consultation of EP)	Initial ceiling: 3,000 mUS$ (revolving fund)	Initial ceiling: 1,000 mUA (to be reviewed after two years) (To this amount must be added part of the loans made in relation to the EMS, as decided by the European Council on 5.12.78 (1,000 mUA per year over a five year period)	The capital of the EIB amounts to 7,000 mUA The statutory ceiling for current loans is 18,000 mUA → idem
5. <u>Guarantee</u> (of the lenders vis-à-vis the Community or the EIB)	ECSC own reserves and guarantee fund (financed by the levy)	EEC budget (Item 3291)	Member States are jointly responsible towards lenders EEC budget could also be used as guarantee (Ch. 42)	EEC budget (Ch. 43)	EIB own resources and capital
6. <u>Interest subsidies</u>	Financed by the yield of the levy. Mainly used for restructuring and reconversion programmes Rate of subsidy: 3%	none	none	none (However loans made in relation to the EMS benefit from a 3% interest subsidy)	none → idem

	ECSC LOANS	EURATOM LOANS	COMMUNITY LOANS (EEC)	INVESTMENT LOANS (EEC)	EIB LOANS
7. Budgetisation	Operations entered in the ECSC "investment budget" which is an internal Commission document	EEC budget: but the precise form and implications of this budgetisation are still being negotiated by Parliament & Council	→ idem	→ idem	The EIB has its own, separated accounts
		(Revenue: Art. 941 Expenditure: Item 3291)	(Revenue: Art. 942 Expenditure: Ch.42)	(Revenue: Art. 943 Expenditure: Ch.43)	
8. Auditing	The Court of Auditors is competent for auditing the ECSC borrowing/lending operations - but this control only gives rise to a report to the Commission and Council and not to Parliament's discharge (Art. 78 f, 5 of ECSC Treaty)	The Court of Auditors is competent for auditing these operations: but the competence of Parliament through the discharge depends upon the exact nature of the "budgetisation" of those operations	→ idem	→ idem	The EIB has its own, separated auditing
9. Volume of operations (mUA) (borrowing)					
- potential	-	1,000	2,143 (or 3,000 m $US)	1,000	18,000 (est.)
- total of borrowing (31.12.1979)	6,256	335	1,816	177	10,580
- 1979 financial year	957	165	-	177	2,480

ANNEX 2

INCREASING THE VOLUME OF THE COMMUNITY'S FINANCIAL ACTIVITIES

The Group considers that the loan issue capacity of the Community should be raised to an annual level of 5,000m EAU.

This position should be interpreted in the light of the following:

- at present, the average annual loan-issue capacity of the Community can roughly be put at:

	(MEUA)
- EIB	2,500
- ECSC	1,000
- NCI	500
- EURATOM	250
	4,250[1]

- an increase in the loan capacity of the Bank - and, to a certain extent, of the ECSC - is subject to specific, autonomous conditions (for example the position of the Bank's capital or of the ECSC guarantee fund); likewise, the use made of these loans is conditioned by specific requirements and rules;

- the bulk of the increase advocated by the Group therefore concerns Euratom loans and NCI loans, the average annual volume[2] of which is in the region of 250m EUA and 500m EUA respectively.

Furthermore, the Group takes the view that the volume advocated, i.e. 5,000m EUA, is, in Community terms, the minimum level required in order to launch a policy of support for productive investments and that this volume should therefore be increased as soon as solid foundations for a common policy in this field have been laid.

---

[1] Loans designed to assist Member States with their balances of payments are of a very special type and are not covered here.

[2] The regulations establishing these loans lay down renewable ceilings of 500m EUA (Euratom) and 1,000m EUA (NCI). It is to be expected that after an initial running-in period, these ceilings will on the basis of an annual loan volume of 250m EUA (Euratom) and 500m EUA (NCI) be reached - and therefore have to be renewed - roughly every 2 years.

	ECSC LOANS	EURATOM LOANS	COMMUNITY LOANS (EEC)	INVESTMENT LOANS (EEC)	EIB LOANS
7. Budgetisation	Operations entered in the ECSC "investment budget" which is an internal Commission document	EEC budget: but the precise form and implications of this budgetisation are still being negotiated by Parliament & Council (Revenue: Art. 941 Expenditure: Item 3291)	→ idem (Revenue: Art. 942 Expenditure: Ch.42)	→ idem (Revenue: Art. 943 Expenditure: Ch.43)	The EIB has its own, separated accounts
8. Auditing	The Court of Auditors is competent for auditing the ECSC borrowing/lending operations - but this control only gives rise to a report to the Commission and Council and not to Parliament's discharge (Art. 78 f, 5 of ECSC Treaty)	The Court of Auditors is competent for auditing these operations: but the competence of Parliament through the discharge depends upon the exact nature of the "budgetisation" of those operations	→ idem	→ idem	The EIB has its own, separated auditing
9. Volume of operations (mUA) (borrowing)					
- potential	-	1,000	2,143 (or 3,000 m $US)	1,000	18,000 (est.)
- total of borrowing (31.12.1979)	6,256	335	1,816	177	10,580
- 1979 financial year	957	165	-	177	2,480

INCREASING THE VOLUME OF THE COMMUNITY'S FINANCIAL ACTIVITIES

The Group considers that the loan issue capacity of the Community should be raised to an annual level of 5,000m EAU.

This position should be interpreted in the light of the following:

- at present, the average annual loan-issue capacity of the Community can roughly be put at:

	(MEUA)
- EIB	2,500
- ECSC	1,000
- NCI	500
- EURATOM	250
	4,250[1]

- an increase in the loan capacity of the Bank - and, to a certain extent, of the ECSC - is subject to specific, autonomous conditions (for example the position of the Bank's capital or of the ECSC guarantee fund); likewise, the use made of these loans is conditioned by specific requirements and rules;

- the bulk of the increase advocated by the Group therefore concerns Euratom loans and NCI loans, the average annual volume[2] of which is in the region of 250m EUA and 500m EUA respectively.

Furthermore, the Group takes the view that the volume advocated, i.e. 5,000m EUA, is, in Community terms, the minimum level required in order to launch a policy of support for productive investments and that this volume should therefore be increased as soon as solid foundations for a common policy in this field have been laid.

---

[1] Loans designed to assist Member States with their balances of payments are of a very special type and are not covered here.

[2] The regulations establishing these loans lay down renewable ceilings of 500m EUA (Euratom) and 1,000m EUA (NCI). It is to be expected that after an initial running-in period, these ceilings will on the basis of an annual loan volume of 250m EUA (Euratom) and 500m EUA (NCI) be reached - and therefore have to be renewed - roughly every 2 years.

IV.

redistribution through budgetary measures

Draftsman: Mr ARNDT

The need for redistribution

1. Whilst economic integration is a process which is certainly of benefit to the Community as a whole, it affords no guarantee that this benefit will be shared by all regions of the Community. In the extreme case, economic integration may even lead to a drop in the prosperity of an area with a particularly unfavourable structure.

2. Redistribution between the Member States must be one of the Community's priority tasks because:

   (a) a reduction of the differences in per capita income and economic performance in the regions is a declared aim of the Community;

   (b) large differences in income and economic performance lead to an undesirable migration from poorer to richer areas.

3. Budgetary measures must be stepped up where the cohesion of the Community needs strengthening, because they are of primary importance for the Community as a whole. There can be no doubt that a widening gap in economic strength and prosperity between individual member countries will jeopardize the cohesion of the Community.

4. Furthermore, a high degree of worker mobility encourages excessive migration from poorer to richer countries, causing considerable harm to both. On the one hand, the workers' countries of origin lose not only a capable workforce but also the considerable educational and social investment which they have made. On the other, the recipient countries also have to commit high expenditure to tackle the problems of congested areas and too large a proportion of Community citizens of another tongue.

4a. The political expectations of the Community's citizens lie mainly in the Community's helping to deal with unemployment and the acute economic situation.

Redistribution: a budgetary responsibility

5. The MacDougall report found that redistribution through public spending and taxation reduced regional inequalities in per capita income by approximately 40% in the countries it studied which had attained a high degree of economic integration (Australia, France, USA and the Federal Republic of Germany).

6. In contrast, the report stated that the redistributive capacity of the Community's finances as between Member States was very low - around 1%. MacDougall considered that the reasons for this were the relatively modest Community budgetary resources suitable for redistribution and the consequently weak geographical redistributive capacity per unit of account.

7. The Council in Dublin expressed its determination to reinforce those policies most likely to favour the harmonious growth of the Member States' economies and to reduce the disparities between them.

8. Redistribution ought to be accorded greater priority within the structure of the Community budget. The various instruments described in this report demonstrate that redistr ibtuion is perfectly feasible.

9. The Commission takes the view that it is not possible systematically to introduce a redistributive element into every single sectoral policy. However, the Commission does say that more consideration should be given to this matter when shaping or reviewing policy in individual sectors.

Instruments and their redistributive effect

10. The European Council was of the opinion that the convergence of economic performances required measures for which the Member States concerned were primarily responsible. Community policies had to play a supporting role within the framework of increased solidarity within the various areas. Steps had to be taken to strengthen the economic potential of the less prosperous countries of the Community. (European Council in Dublin).

11. The present report is primarily concerned with the tasks that the Community's finances can accomplish in order to reduce differences in per capita income and the structural gap between Member States and/or individual regions in the Community. Greater convergence of economic development in the individual Member States is one of the principal aims of the Community.

12. Any financial arrangements for redistribution must accept the fact that

(a) the system of own resources is inviolable, and
(b) no Member State has the right to recover all the resources it has contributed ('juste retour').

13. The redistributive effect of revenue is very slight since neither customs duties and agricultural levies nor contributions geared to gross national product lend themselves to this kind of operation. Only the calculation of value added tax revenue has a certain redistributive effect.

14. However, even on the expenditure side there are only a few quite specific policies which can be used to achieve redistribution.

15. Within the context of the present Community set-up it would seem that the best way to achieve redistribution is to provide grants for specific purposes such as regional policy or employment assistance programmes. Direct redistributive measures on a broader scale are less appropriate because lasting convergence will only be brought about by changing the structures of the disadvantaged areas. A lower

financial contribution from an individual Member State or a direct grant not earmarked for any particular purpose will do nothing to alter the economic structure of a disadvantaged area.

16. The MacDougall report too argued that inequality in per capita income is reduced by activities in the field of structural and cyclical policy. Regional policy, job creation programmes and employment policy should, it said, as far as possible ensure that the benefits of integration are enjoyed by all, that the convergence of economic development in all Member States should increase or that, at least, the divergence should not become wider.

Horizontal financial equalization

17. According to the MacDougall report, a system similar to the 'Länderfinanzausgleich' in Germany, given 2% of the total gross national product of the Community, could raise the per capita fiscal capacity of the economically weaker Member States to a minimum of 95% of the Community average.

18. In the opinion it issued on the MacDougall report, the Commission raised the question whether there would have to be a reallocation of responsibilities in the Community's favour. The Commission considers that a transfer of certain tasks to the Community could reduce public spending and that other expenditure would of necessity have to be transferred to the Community.

Revenue-raising system with progressive effect

19. In order to meet the demand for an increase in own resources and fiscal equalization, a proposal has come from many quarters (including the MacDougall report) that a progressive revenue-raising source be created.

20. Firstly, the ceiling of the Community's VAT revenue would be raised from 1% to 1½% or 2%. Secondly, the VAT revenue should be calculated using a formula with built-in progression. The result of this would be that States with a high VAT yield would have to pay a percentage which rose proportionately more steeply.

21. The formula thus has two elements only one of which however need be applied in any one case. The first is the size of the Member State, which largely determines the level of the VAT yield so that larger States pay more per capita than the smaller ones. The second is economic strength, which also has a decisive influence on VAT yield, so that the economically stronger States pay more per capita than the weaker ones.

Fiscal equalization by means of general purpose grants

22. Several States constructed on the federal principle have a system under which, in addition to specific purpose grants, general purpose financial transfers are made from the central government to the regional government or there is horizontal equalization between regional governments. These equalization arrangements can have a very marked redistributive effect.

23. One good example of this is the system of fiscal equalization carried out between the federal government and the Land governments in Germany. The system comprises three adjustments to the allocation of tax yields.

24. (a) Part of the VAT revenue is not distributed according to the place of its collection but it is used to raise the fiscal capacity of all the Länder to a minimum of 92% of that of the Federal Republic as a whole.

25. (b) Further equalization is effected from tax revenues between the Länder. The richer Länder (e.g. Hessen and Hamburg) make payments to the poorer ones (Rheinland-Pfalz, Schleswig-Holstein) until their fiscal capacity reaches the minimum of 95% of that of the Federal Republic ('Länderfinanzausgleich').

26. (c) Finally, the Federal Government raises, by means of supplementary grants, the minimum fiscal capacity of the poorer Länder by another 2% to 97% of the federal average.

Arguments against general purpose grants

27. Redistribution between States not earmarked for a specific purpose presupposes by its very nature a high degree of economic and particularly institutional integration. In all federations which effect a high level of redistribution by means of horizontal non-specific grants, the powers of the federated states clearly give ground to those of the central government. Those who wish to pursue the course of redistribution for other than a specific purpose, e.g. on the principle of 'juste retour' should logically therefore be prepared to have some of the Member States' sovereign rights transferred to Community institutions.

28. The concept of the Community laid down in the Treaties therefore clearly does not accord with non-specific payments to the Member States.

29. Only a very extreme situation could justify a limited scheme of non-earmarked redistribution. As an example of this the MacDougall report postulates the case where a Member State may find itself with less than 65% of the Community's average fiscal capacity. The report states that such a system might ensure for poor, small and peripheral Member States standards not too far below those of the main body of the Community.

An exception: the 'financial mechanism'

30. The financial mechanism set up by the Council regulation on 17 May 1976 provides that a Member State which finds itself in a special economic situation and whose financial contribution is a disproportionate burden on its economy, may receive a payment from the Community budget.

31. The conditions for such a payment are that

(a) the per capita gross national product is less than 85% of the average per capita GNP for the Community;

(b) the growth rate of the per capita GNP of the Member State in real terms is less than 120% of the average rate for the Community; and

(c) the proportion of the Community's income made up by the Member State's financial contribution exceeds that State's share of the Community's total GNP by more than 10%.

32. This financial mechanism does not encroach upon the system of own resources since it defines a very specific exceptional situation and furthermore limits the size of the payment through additional provisions.

33. The Commission considers that the financial mechanism must be developed further since its scope and effect are too limited and hence the two conditions added subsequently should be abolished.

34. These conditions are:

(a) that the payments made under the financial mechanism shall not exceed 3% of budgetary expenditure;

(b) that the payment to the Member State concerned shall not exceed the value added tax paid over by it or the net transfers it shall be required to make.

Expenditure with high redistributive effect

35. The MacDougall report gives particular attention to the following possible measures to reduce differences within the Community:

(a) more expenditure in the form of regional policy aids (employment or investment incentives, public infrastructure, urban redevelopment);

(b) more expenditure for labour market policies (vocational training and other employment measures);

(c) a limited budget equalization scheme for extremely weak Member States whose fiscal capacity lies substantially below the Community average.

36. The report then suggests that a sum of 10,000 million EUA allocated to these measures could reduce inequalities in living standards between Member States by about 10%.

37. The MacDougall report comes to the conclusion that the main need for macro-economically significant expenditure is in the area of structural, cyclical, employment and regional policy.

38. The Commission has issued a guideline for expenditure on structural policy listing the various projects involved in order of importance. Action will be taken in the areas of

regional policy
interest subsidies for poorer countries,
employment policy, and
policy on agricultural structures.

39. The Commission has also made it clear that the resources for the Regional Fund must be raised by an adequate amount and that the resources over and above the quota-linked share which are at present limited to 5% of the Regional Fund must also be increased.

The link between redistribution, agricultural expenditure and the budget

40. There is a direct link between the convergence of economic performance, curbing the rise in agricultural expenditure and enlarging the financial framework. With agricultural expenditure continuing to rise, the room for manoeuvre within the 1% limit for expenditure having a redistributive effect which might solve the problems of convergence is becoming increasingly narrow.

41. The Commission therefore takes the view that the Community's aim of increasing the share of its expenditure which goes to investment and structural improvement projects will only be reached if the Community can succeed in curbing its agricultural expenditure.

42. The Community's expenditure on agriculture has no redistributive effect between rich and poor Member States, since the objectives it pursues are purely sectoral ones.

43. As long as budgetary expenditure not suited to redistribution is four or five times greater than expenditure having a redistributive effect, the convergence called for by Council, Commission and Parliament will remain no more than a distant prospect.

44. Parliament has accordingly often stated that Community policies in their present form are incapable of creating the degree of convergence between the national economies necessary to promote the cohesion and progress of the Community. In Parliament's view

(a) the lack of convergence lies at the root of the Community's serious problems, and

(b) the statements made by the Council on the need for convergence have so far borne no fruit because of the absence of a political will.

CONCLUSIONS

45. In the conviction that

- a reduction of the differences in per capita income and economic performance is a declared aim of the Community,

- the widening gap in economic strength and prosperity between member countries will jeopardize the Community's cohesion, and

- the present redistributive capacity of the Community is infinitesimal,

the European Parliament calls for the aim of redistribution to be accorded greater priority within the structure of the Community budget.

46. In the conviction that

- the system of own resources is inviolable,

- no Member State has the right to recover all the resources it has contributed,

- the present calculation of value added tax revenue has no redistributive effect,

- non-specific payments to the Member States can achieve a slight redistributive effect only in extreme cases, and

- large blocks of expenditure such as the Agricultural Guarantee Fund have no redistributive effect and may even be counter-productive,

the European Parliament calls for

(a) the graduation of value added tax revenue according to gross domestic product expressed in terms of per capita purchasing power,

(b) the additional graduation of value added tax revenue according to the size of population, and

(c) a substantial increase in the proportion of expenditure with a strong redistributive effect in the Community budget.

47. In view of the fact that the proportion of Community revenue from value added tax which the individual Member States have to contribute differs markedly from the respective share of total gross domestic product, the European Parliament proposes

(a) correcting the value added tax yield by a coefficient with a redistributive effect based on the above- or below-average level of gross domestic product expressed in per capita purchasing power,

(b) calculating this coefficient in such a way that each Member State's deviation from the Community average is established, and then

(c) increasing, or decreasing, the value added tax amount for each individual Member State, expressed as 100, by a tenth part of this deviation.

(for sample calculation, see Table 1)

48. In view of the fact that Member States with larger populations may be relatively better able to bear the burden, the European Parliament proposes

(a) correcting the value added tax yield by means of an additional coefficient based on the above- or below-average proportion of the total Community population figure,

(b) calculating this coefficient in such a way that each Member State's deviation from a national average of 10% of the total population is established, and then

(c) increasing, or decreasing the value added tax amount for each individual Member State, expressed as 100, by a tenth part of this deviation.

(For sample calculation, see Table 2)

49. In the conviction that

- the aim of redistribution is best achieved by payments for quite specific purposes,

- lasting convergence will only be attained by changing the economic and social structure of disadvantaged regions,

- direct, non-specific grants do not change the economic structure of a region, and

- expenditure suited to redistribution forms a much too small proportion of total expenditure,

the European Parliament calls for a marked increase in expenditure in the fields of

(a) regional policy (on employment and investment incentives, public infrastructure, and urban redevelopment)

(b) employment policy (on vocational training and other employment measures)

(c) structural policy and

(d) cyclical policy.

VAT WEIGHTING MECHANISM

ANNEX

Table 1

	Gross domestic product	± EEC average	coefficient
Belgium	4.68%	+ 23%	102.3%
Denmark	2.72%	+ 38%	103.8%
Germany	31.75%	+ 35%	103.5%
France	23.66%	+ 15%	101.5%
Ireland	0.63%	- 50%	95.0%
Italy	13.4 %	- 38%	96.2%
Luxembourg	0.17%	+ 21%	102.1%
Netherlands	6.34%	+ 18%	101.8%
United Kingdom	16.65%	- 22%	97.8%

Table 2

	Share of population	deviation from 10%	coefficient
Belgium	3.79%	- 6.21%	99.4%
Denmark	1.97%	- 8.03%	99.2%
Germany	23.56%	+ 13.56%	101.4%
France	20.55%	+ 10.55%	101.1%
Ireland	1.26%	- 8.74%	99.1%
Italy	21.90%	+ 11.90%	101.2%
Luxembourg	0.14%	- 9.86%	99.0%
Netherlands	5.39%	- 4.61%	99.5%
United Kingdom	21.45%	+ 11.45%	101.1%

Table 3

The formulas combined

Belgium	101.7%
Denmark	103.0%
Germany	104.9%
France	102.6%
Ireland	94.1%
Italy	97.4%
Luxembourg	101.1%
Netherlands	101.3%
United Kingdom	98.9%

Table 4

Effect of formulas 1, 2 and 3 on the 1980 budget (in m EUA)

	Preliminary draft	coeff. 1	coeff. 2	coeff. 3 (1+2)
Belgium	304	311	302	309
Denmark	176	182	174	181
Germany	2,195	2,272	2,225	2,302
France	1,652	1,676	1,669	1,694
Ireland	57	55	57	54
Italy	729	702	738	711
Luxembourg	14	14	13	14
Netherlands	405	413	403	411
United Kingdom	1,162	1,136	1,175	1,149
	6,694	6,761	6,756	6,825

V.

new own resources for the Community

Draftsman: Mr SPINELLI

------

1. Introduction

The present document enlarges upon the chapter of the working party's programme entitled 'new resources' and makes use of the analyses of the financing of the Community budget provided in the Commission's communication of 21 November 1978.

In the working party's programme it had been agreed (see minutes PE 62.658) that the new own resources would have to meet the following requirements:

(a) the total burden on Community taxpayers should, in principle, not be increased;

(b) the Community's fiscal system must become progressively fairer;

(c) the principle of equity must be applied not so much to the share of the Community budget to be founded by each Member State but to the type of fiscal burden placed upon Community citizens.

2. General

The Decision of 21 April 1970 envisages that the Community's budget should be financed by own resources. The expression 'own resources' means revenue of a fiscal nature belonging once and for all to the Community as of right for financing its budget without the need for any subsequent decision by national authorities.

As from the 1980 financial year, the Community's budget will be financed completely from:

(a) own resources of a commercial nature (customs duties and agricultural levies);

(b) resources of a fiscal nature in the strict sense of the word (VAT and taxes on staff salaries);

(c) resources of a parafiscal nature (coresponsibility levy and sugar contributions).

The ECSC budget which is separate from the Community budget is mainly financed from resources of a parafiscal nature.

When the budgetary procedure for 1978 was under way, Members of Parliament from various political groups, had already called the Commission and Council's attention to the possibility that the Community's own resources might be exhausted in the short term and the need to begin a detailed examination of the Community's future fiscal system as quickly as possible.

In response to these remarks and to the financial estimates contained in the three-year forward forecasts for 1979-81 and 1980-82 the Commission submitted a communication to the Council and the EP in which it stated that:

(a) there is a real possibility that the 1% VAT ceiling may be exceeded in 1981;

(b) it is essential to find new sources of revenue;

(c) the additional revenue must be found exclusively from within a range of taxes which have the full character of own resources;

(d) VAT is a good basis for the creation of new revenue since a raising of the present ceiling would have the advantage of simplicity;

(e) a study should nevertheless be made of the feasibility and most suitable methods of introducing progressive elements into the Community's fiscal system.

When presenting its opinion on the three-year forward forecasts 1979-81 to the Council and the Commission, the Economic Policy Committee had for its part noted that:

> 'the Commission will present a report on new own resources for the Community'

and stressed:

> 'the need for immediate and careful consideration of this topic in view of the time factor and the problems involved in having any amendment to the Decision of 21 April 1970 drawn up, discussed and adopted by the Community's institutions and then ratified at national level'

Furthermore, in the three-year forward financial forecasts for 1980-1982, the Commission emphasized that in 1980 the yield from customs duties would begin to be affected by the tariff reductions decided within the GATT which are to be staggered over a period of eight years. Over the same three years there would also be a decline in the revenue from agricultural levies.

The Commission has put forward **two hypotheses**: (i) that agricultural expenditure (EAGGF Guarantee Section) might be brought under control, in which case the yield from VAT would still cover the totality of budgetary expenditure in 1982 although the problem would be encountered shortly thereafter; or (ii) an automatic and steady rise in this expenditure comparable with the growth of expenditure since the creation of the common agricultural market. Should this be the case, the Commission has warned the budgetary authority that expenditure will inevitably exceed the maximum yield from VAT from 1982 onwards.

The trend in agricultural expenditure since the rejection of the draft budget for 1980 and the presentation of the Gundelach package might now give the impression that the danger of own resources proving insufficient in the short term has been receding.

The Commission, in its working paper on the 'trend in agricultural expenditure and its effect on the Community budget' (SEC(80) 419) states that this impression would be wrong since the present situation leaves very little room for manoeuvre. The Commission concludes in the light of the considerations set out in this that 'it is clear that the trend in expenditure is necessitating ever greater use of VAT-derived own resources. Moreover, the rate of use will inevitably rise towards the upper limit, the 1% ceiling'.

In addition, it should be emphasized that the procedures laid down for granting the Community further own resources different from this it already holds are long and complicated.

3. Two political premises

The need to tackle the problem of finding more adequate financing for the Community budget immediately is confirmed by the conclusions reached in the working documents drawn up by Mr BARBI and Mr ARNDT. These conclusions do moreover accord with the European Parliament's political pronouncements on 'convergence and budgetary questions' (resolution of 15.11.1979. - rapporteur: Mr LANGE) and the rejection of the 1980 draft budget (resolution of 13.12.1979. - rapporteur: Mr DANKERT).

Mr Barbi, who starts out from the notion that most Community expenditure is a replacement for national expenditure, acts as a multiplier and encourages economies of scale, concludes by stating that the Community's policies will only be fully effective once the threshold of 2.5% of the total gross national product of the Community has been passed.

Mr Arndt says that, in order to be able to deal with the problems raised by the development of the Community and the question of fairer participation in the Community by the Member States in terms of their citizen's contributions, the VAT ceiling must be raised from 1% to 1.5% or 2% and the formula used for calculating VAT revenue should have built-in progression.

4. <u>Financial autonomy and the unity and comprehensiveness of the budget</u>

A third political premise is that the choice made with the Decision of 21 April 1970 to finance the Community budget exclusively from own resources is irreversible. Accordingly, the Community's institutions must make it their task to safeguard the Community's financial autonomy at all times.

Furthermore, with the sole exception of the agricultural sector in which resources of a parafiscal nature will be used to meet specific items of expenditure, the Community's institutions must devote themselves to safeguarding the principles of the <u>unity</u> (expenditure is derived from revenue) and <u>comprehensiveness</u> (all revenue and all expenditure must be entered) of the Community's budget.

5. <u>Basic criteria for financing the EEC budget</u>

There are essentially two ways in which an adequate medium-term solution can be found to the problem of financing the Community's budget:

(a) allocating to the Community a partial or total rate of one or more of the taxes <u>already existing</u> in the Member States;

(b) the creation of one or more <u>new</u> taxes, implying an additional fiscal burden on Community citizens.

Today's national fiscal systems are to complex and multi-faceted that it is practically impossible to create a tax which is different from those already in operation except perhaps some minor excise duty and hence option (b) exists only in theory.

Option (a) however would require the progressive harmonization of the basis of assessment of the taxes from which a rate would in whole or in part be transferred to the Community. This what was done to enable a share of VAT revenue to be allocated to the Community.

6. <u>The objectives of the Community's future fiscal system</u>

The volume of the Community's own resources in the medium-term will be marginal in comparison with national public expenditure and the overall level of taxes raised by the Member States.

When one considers that the total amount raised by the Member States in taxation today is equal to approximately 36.6% of the Community's total gross domestic product and that several authorities have indicated that 2.5% of this GDP is the critical threshold which the Community's budget will have to reach, it follows that in the medium term the Community's fiscal take will reach a figure of approximately 7% of the total amount raised in taxes by the Member States.

Bearing this in mind it is only realistic to say that in the medium term the Community's fiscal policy will not be in a position to serve such objectives as the redistribution of income, the variation of aggregate demand or a policy of investment stabilization and incentives which are normally pursued by national fiscal policy.

The two principal objectives of the Community's fiscal system for the time being would therefore seem to be:

(a) to have available the largest possible tax revenue in order to meet the Community's growing financial requirements over the medium term;

(b) to achieve overall a fairer fiscal system for individual Community citizens and for the citizens of each Member State taken as a group by introducing strong progressive elements.

7. The instruments of the Community's fiscal policy

There are three:

(i) Definition of the assessment base of those taxes for which a rate will be allocated in whole or in part to the Community. This must be done in accordance with the Community procedure already used for the harmonization of the basis of assessment for VAT.

(ii) Assessment of taxable income. This requires a strengthening of the auditing procedures carried out by the Community and closer cooperation between national and Community fiscal authorities to combat tax evasion and avoidance.

(iii) Collection of fiscal revenue. In the medium term the collection of Community's fiscal revenue can continue to be carried out by the Member States which will act as the Community's agents - as they do already in the case of levies, the VAT rate and customs duties -.

The Community's fiscal system must also have the following basic characteristics:

(a) Community taxes must be collected as far as possible directly from the taxpayer;

(b) Community taxes must be recognized as such by the taxpayer;

(c) there must be no new fiscal bureaucracies;

(d) the harmonized basis of assessment must be as simple as possible.

8. The harmonization of national fiscal systems

The convergence of national fiscal systems is one of the most important stages in the realization of a genuine common market and the other objectives which the Community has set itself.

The harmonization of national fiscal systems has been under consideration by Community institutions ever since the presentation of the Neumark Report in February 1963 on the 'fiscal and financial harmonization of the Common Market'. The Commission later submitted fiscal harmonization programmes having particular regard to direct taxation, first in 1967 and then in 1975.

The European Parliament delivered a detailed opinion on the basis of the report presented by Mr Artzinger on behalf of the Committee on Budgets during the 1974-1975 session on 'the fiscal harmonization of the Member States'.

Furthermore, the Council of Ministers, in the resolution it adopted in March 1971 on the establishment of Economic and Monetary Union, had already declared that:

'to accelerate the introduction of the free movement of persons, groups, services and capital and the interpenetration of the economies, the Council shall, on a proposal from the Commission, decide on an appropriate package of measures concerning:

- the Community rules determining the uniform basis of assessment for value-added tax in accordance with the Decision of 21 April 1970;
- the harmonization of the scope and, basis of assessment of and rules for levying excise duties and particularly those having a significant effect on trade;
- the harmonization of some types of tax which may have a direct influence on capital movements within the Community and in particular the harmonization of the tax arrangements applicable to interest from fixed-interest securiti and dividends;
- further harmonization of the structure of company taxation;
- a gradual increase in duty-free allowances for citizens crossing Community frontiers.

Before the end of the first phase, the Council will examine the studies to be carried out in accordance with the Commission's proposals concerning the approximation of the rates of value-added tax and excise duties'.

The harmonization of national fiscal systems is essential for the future financing of the Community budget for two reasons:

(a) the allocation to the Community of part or all of a given rate of national taxes requires gradual harmonization of their bases of assessment;

(b) the development of the Community's fiscal system in the medium term requires:

(i) a harmonization - not necessarily absolute but certainly advanced - of the rates of the national taxes which are in part transferred to the Community;

(ii) in order to prevent distortions within the national fiscal systems (having regard to the fact that the amount raised in taxation by the Community must reach at least 7% of the total raised by the Member States), greater convergence will be needed in the relationship between the various types of obligatory payments (taxes and social welfare contributions) within national fiscal systems.

Although protracted procedures will have to be followed before these various factors can be harmonized with action having to be taken by the Community's institutions, political organizations, governments, national civil services and national parliaments, the ultimate objective is not so difficult to attain and the emphasis placed on the difficulties is for the most part due to opposition from those who fear that they will lose influence or vested interests and to ways of thinking which must also be changed.

In fact, although the make-up of taxation does differ considerably from one Member State to another, it is also true that there are some common trends, for example the steady shift away from indirect taxation in favour of direct taxation.

There is greater divergence between the Member States' arrangements governing social welfare contributions, but this is not relevant to the discussion here.

Finally, it should be borne in mind that, following the Decision of 21 April 1970, the Community's institutions were able to start work on the harmonization of the basis of assessment of the most important indirect tax, VAT, and that this has largely now been achieved.

9. The choice of new Community taxes

The creation of new own resources will be a long process and there is therefore a need for a short-term project to ensure the financing of the Community's budget over the next few years.

The practical solutions over the short term, as outlined recently by the Commission, are as follows:

(a) an increase in the rate of VAT revenue allocated to the Community (from 1% to 2% or by abolishing the ceiling). This would require an amendment to Article 4 of the Decision of 21 April 1970 by means of the Community procedures for revising the Treaties;

(b) widening the range of 'resources of a commercial nature' (customs duties and agricultural levies) by introducing, for example, a duty on imports of oil into the Community or duties on imports of vegetable oils. This can be done by means of the simple Community procedure, i.e. a proposal from the Commission, an opinion from the European Parliament and a decision from the Council.

Solution (a) (an increase in VAT) would have considerable advantages and could be used for financial equalization in the way proposed by Mr Arndt in his working document. However, VAT does not have a progressive effect which can be applied to individual taxpayers, and the financing of the Community budget in the medium term exclusively from resources of a commercial nature and resources derived from indirect taxes alone could give rise to considerable distortions.

The only advantage of solution (b) (the introduction of new taxes) is that it can be introduced more easily by means of a decision taken by the Community institutions. Nevertheless, a tax on oil imports or duties on vegetable oils would both have extremely negative side-effects which militate against the use of these resources for the future financing of the Community budget.

As far as the tax on energy imports is concerned, the Commission, in its communication to the Council on a 'Community energy initiative' (COM(80) 130 final) has examined the possibility of introducing a Community tax on energy to help achieve the overall objectives of the energy policy.

The Commission considers that it would be desirable to:

- adopt a system which would be simple to administer, would create the fewest political and constitutional difficulties, and which could be introduced rapidly;

- minimize complications with third countries, particularly oil-producing countries, and those with which the Community has concluded preferential agreements;

- transform the tax into Community own resources, the revenue from which would go directly to the Community budget.

According to the Commission the main fiscal instruments would be:

- either a tax on energy consumption in all its forms;

- or a tax on oil and specific oil products;

- or a tax on energy production in general or just oil production;

- or a customs duty;

- or a levy on energy imports in general or only on oil;

- or a levy on particular oil products.

The Commission has promised to submit to the Council a detailed study of the various schemes which might possibly be used to raise revenue from the energy sector.

In its communication on 'financing the Community budget' of 21 November 1978, the Commission had previously stated that 'a Community tax on the production of energy would not be consistent with the energy policy objectives of stimulating production'.

The Commission pointed to the need to take account of economic effects of a tax on consumption and the great difficulties of harmonizing such a tax.

The reference to the simplicity of administration and the political and constitutional procedures clearly shows that the Commission favours a duty on energy imports.

It is therefore felt that the introduction of an import duty on oil can be envisaged solely as one element of an overall Community energy policy.

Turning to the duty on vegetable oils, the Commission noted in its communication to the Council on 'changes in the common agricultural policy to help balance the markets and streamline expenditure' (COM(79) 710 final) that a more coherent policy on animal and vegetable fats might become necessary, particularly in the context of enlargement. The Commission feels that this can only be brought about by imposing a levy on vegetable fats produced in the Community or imported from third countries.

In order to ensure that this levy would not be discriminatory, would not require the destruction of produce and would be simple to administer, the Commission is in favour of making the following provisions:

(a) that the levy should be applied to oil seeds and oleaginous fruit, both originating in the Community and imported, as they are processed in preparation for olive oil production;

(b) that the levy should be applied to imported oils and fats and imported products containing large amounts of oil, as they enter the Community;

(c) that the levy should be fixed in absolute terms once a year and that the same figure should be applied to all oils and fats;

(d) that the levy should be refunded where the produce is exported or used for purposes other than human consumption.

It should be strongly emphasized that this type of resource has the following drawbacks:

(a) in a period of gradual liberalization of trade, a tariff of this kind would strengthen the Community's agricultural protectionism;

(b) it would particularly harm relations with the developing countries towards which the Community has assumed and will assume international, inter-regional and bilateral commitments regarding a wider Community preference for their agricultural exports;

(c) it is illogical that olive oil which is already in difficulty and receiving subsidies should be subjected to a further tax increase;

(d) not only would the protectionism of the Community's agricultural policy be strengthened, but also the Community might be forced to make significant concessions in compensation to its trading partners within GATT which would increase their protectionism;

(e) an increase in the price of margarine and vegetable oils would encourage a further increase in butter production which would have a harmful effect, for example, on the health of Community citizens since the consumption of vegetable fats is always preferable to that of animal fats.

The conclusion to be drawn from these considerations is that Community institutions, political organizations and the governments of the Member States must immediately (to allow the objective to be attained in the medium term) tackle the problem of transferring part of the revenue from existing national direct taxation to the own resources of the Community since this is the only means of ensuring a high degree of fiscal equity.

The political hypothesis which the European Parliament ought to be urging the other Community institutions to accept is that of a progressive harmonization of the bases of assessment of direct taxes on the income of natural persons, accompanied by an acceleration of the harmonization of taxes on dividends and company taxation which has been under way for some time.

This harmonization is vital if the Community is to be able to use as an own resource the yield from a Community rate applied to direct taxation on the income of natural persons.

The process of convergence between national fiscal systems described in section 8 above, will also require - in the long term - a large measure of harmonization of the rates of direct taxation on persons.

Clearly the harmonization of VAT rates and the rates of direct taxation will have an effect on each other since these are the most important elements of the national fiscal systems.

10. Conclusions

The working party draws the following conclusions from the above considerations:

(a) to allow further progress towards Community integration and more efficient management of the common policies greater scope will have to be found for financing the Community budget;

(b) the revenue for the Community budget must be drawn exclusively from a system of genuine own resources;

(c) the evenue for the Community budget must come from a partial or total allocation to the Community of a given rate of one or more taxes already existing at national level which does not thereby increase the overall fiscal burden on the taxpayer;

(d) the Community's fiscal system must be a fair one both as regards the burden on the individual citizen and on the citizens of each Member State as a group (the Arndt proposal);

(e) the Community's taxes must be chosen from amongst the taxes existing at national level providing a sufficiently high yield to allow the financing of the Community budget to meet future developments;

(f) in the short term there must be a change in the rate of VAT revenue allocated to the Community under the Decision of 21 April 1970;

(g) in the medium term there must be: (1) harmonization of the basis of assessment for direct taxation on the income of natural persons; (2) the allocation to the Community of a given rate of these taxes; (3) harmonization of the rates of indirect taxation (VAT) and direct taxation (natural and legal persons);

(h) Community taxes must be collected directly from the taxpayer and not by means of the 'statistical method'.

VI.

the decision-taking machinery for the
Community's own resources

Draftsman: Mr NORD

INTRODUCTION

1. This document takes a stage further the ideas summarized in the chapter of the working party's programme of work dealing with decision-taking machinery. Taking as its starting point the present situation with regard to the Community's own resources, the document attempts:

(1) to clarify the question of the availability of Community own resources,

(2) to adapt the rules for the alteration and creation of own resources to meet new developments since 1970,

(3) to set up a new system for regularly reviewing the Community's financing requirements.

I. AVAILABILITY OF OWN RESOURCES

(a) The so-called 'depletion' of own resources

2. Since the entry into force of the Community VAT[1] and given the fairly high level of the latter within the 1% 'ceiling', there has been much talk about the Community's own resources running out. Some Member States consider that this ceiling represents the maximum financial resources available to the Community, at least in the foreseeable future and that it therefore governs the amount of planned expenditure.

3. The desirability of undertaking new activities - and even of expanding existing policies - has thus come to be assessed more and more on the basis of the resources available within the 1% ceiling. The Council has already decided not to undertake certain priority or even urgent measures so as to remain within the ceiling. There is therefore a risk of the Community becoming a sort of 'Limited company with a share capital of 1% of VAT'.

This concept is totally unacceptable and contrary to both the letter and the spirit of the Treaties.

(b) The 'open-ended' nature of Community financing

4. The Treaty assigns the institutions a number of objectives, the attainment of which requires corresponding financial resources. While the relative availability of such resources may admittedly influence the rate of progress towards these objectives, it would not appear possible within the spirit of the Treaties to arbitrarily impose a ceiling on resources which would effectively limit any further development of Community activities.

5. The financial provisions of the Treaty, although now partially obsolete[2], lay down the following rules:

---

[1] Partially in 1979 and wholly in 1980

[2] See paragraphs 14 to 17 below

- Article 199 states that revenue and expenditure should be in balance,

- Article 200 specifies the available resources,

- Article 201 lays down the procedure for creating new resources or altering existing resources,

- Article 203 sets out the rules governing the adoption of the budget, i.e. decisions on expenditure.

6. There can be no question of introducing any form of mandatory ceiling on resources, given this machinery and the fact that the whole Community venture must necessarily be evolutionary in character.

(c) The significance of the 1% of VAT 'ceiling'

7. Under these circumstances, how is the decision of 21 April 1970, which at the same time as replacing Member States' contributions by own resources laid down that the rate of Community VAT should not exceed 1%, to be interpreted?

8. This limit should not be seen as either permanent or absolute but rather as a phase preceding the normal operation of the Community VAT system. After a trial period for this new form of revenue any restrictions must be removed so that the rate is left free to fluctuate as required.

9. In practice the system of levying a proportion of VAT - which should have been introduced from 1 January 1975 - was applied to all the Member States only with effect from 1 January 1980. As a result the proportion of VAT levied has from the very outset been near the 1% limit and the trial period originally planned is liable to be much shorter than foreseen. This may lead some people to consider fixing a new 'ceiling' (e.g. 2%), and thus extending the trial period.

10. The author does not share this view, believing instead that the original schedule should be adhered to and that once expenditure has grown in the normal way to over 1%, the relevant authorities should propose total abolition of the ceiling.

(d) Abolition of the 1% ceiling

11. The Commission should therefore in due course put forward a very simple proposal to amend the decision of 21 April 1970. The amendment would involve deleting from the second subparagraph of Article 4(1) the words underlined below:

'.......
Such resources shall include those referred to in Article 2 and also those accruing from the value added tax and obtained by applying a rate not exceeding 1% to an assessment basis which is determined in a uniform manner for Member States according to Community rules ......
.......'

II. THE DECISION-MAKING PROCESS FOR THE CREATION/ALTERATION OF OWN RESOURCES

12. In addition to the above question of removing the ceiling on VAT, the working party as a whole will have to decide on whether or not proposals should be made to alter the present system of own resources or to create new resources.

13. This working document merely considers whether the procedure laid down in the Treaties for the creation or alteration of such resources should be reviewed in the light of developments since 1970.

(a) The need to update Articles 200 and 201 of the EEC Treaty

14. It is quite clear that parts of Articles 200 and 201 have become obsolete since the Community system of own resources was introduced by the decision of 21 April 1970.

15. Article 200 states that the budget revenue shall be financed from contributions from the Member States according to certain scales[1].

16. The first paragraph of Article 201 states that these contributions could be replaced by own resources in particular by revenue accruing from the Common Customs Tariff.

17. These two articles are clearly outdated. They could in fact have been revised when the Treaties were amended in 1975 to increase Parliament's budgetary powers. It is now essential that they be updated.

(b) Revising the procedure for creating or altering own resources

18. The third paragraph of Article 201 lays down the procedure for replacing national contributions by own resources. This procedure is also therefore applicable to any alteration or creation of own resources since 1970.

The procedure provides for:

- a Commission proposal,
- consultation of the European Parliament,
- unanimous decision by the Council,
- ratification by the Member States.

19. The following changes in the respective powers of the Community institutions since 1975 would appear to justify alterations to the decision-making process:

- since 1975 Parliament has become a budgetary authority in its own right working in conjunction with the Council;

- since 1979 Parliament alone directly represents all the citizens, and hence all the taxpayers, of the Community;

---

[1] The scales refer only to the six original Member States (see Annex I)

- as from 1980 the budget has been entirely financed by resources raised directly by the Community.

20. It would therefore seem that the 'ratification' of Council decisions on own resources should henceforth be a matter not for the Member States but for the European Parliament. Indeed, in 1973 the Commission drew up proposals for revising the Treaties[1] along these lines. It proposed the following procedure for the alteration or creation of own resources:

- Commission proposal,
- unanimous agreement of the Council,
- decision by Parliament by a majority of members and three-fifths of the votes cast.

21. This proposal was never considered by the Council, which claimed that the problem of the establishment of new resources was not of immediate concern; the Council did however concede that this amendment raised a problem which could be examined later[2]. The proposed revision is therefore still on the table and could be re-activated by Parliament.

22. It should be pointed out that removal of the need for ratification by the Member States does not fundamentally alter the political balance as the agreement of each Member State (by unanimous vote in the Council) is still required to create or alter own resources. Removal of the need for ratification by Member States would however do away with the lengthy delays (two to three years) required for approval by national Parliaments.

(c) Application of the amended decision-making procedure to the question of abolishing the ceiling on VAT

23. Could the decision-making procedure be revised - by means of amendment of the Treaties - before any decision to remove the ceiling on VAT? This would obviously depend on how pressing the latter problem became, namely on how soon the annual rate of VAT reached the 1% ceiling. This is still unclear.

24. If it became necessary to decide to abolish the ceiling on VAT before the Treaties were revised, such a decision should obviously be taken only after detailed consultation between the Parliament and the Council.

III. PLANNING AND PERIODIC REVIEW OF THE EEC's FINANCING REQUIREMENTS

25. In addition to the removal of the ceiling on own resources and revision of the decision-making procedures, there would seem to be a need for effective forward planning of the future pattern of the financing requirements - i.e. the resources - of the Community over a three to five-year time scale.

---

1 See Annex II

2 See Doc. 213/74

26. Such planning would fulfil two objectives:

- provision of the fullest possible information for the budgetary authority on the medium-term growth pattern of the various own resources in the light of economic and commercial developments;

- a detailed review at regular intervals of the operation of the whole system of own resources.

(a) Study of the future pattern of own resources

27. Given the now substantial volume of Community resources, there would seem to be a need for a more detailed and systematic method of forward planning of the future pattern of the various resources so that the budgetary authority is kept better informed of the medium-term financing possibilities for Community activities.

28. This exercise would involve estimating as accurately as possible

- the future pattern of trade-linked resources (levies and customs duties) in the light of foreseeable developments in prices, customs tariffs, the trade cycle, etc. ...

- the future assessment basis for Community VAT - and hence the yield of the Community rate - as influenced by general economic activity and inflation;

- the future pattern of all Community own resources compared to the respective GNP and budgets of the Member States.

29. Planning could cover a three-year period and be rolled forward each year. A similar system already exists for expenditure in the form of the triennial estimates drawn up by the Commission each year when preparing the preliminary draft budget.

This system could simply be extended to cover revenue as well.

30. These forecasts would, however, have to be kept separate from the budget procedure itself and should be made in conjunction with the 'Comprehensive review of budget problems' which is carried out separately at the beginning of each financial year[1].

31. Parliament must be fully involved in both the expenditure and revenue aspects of this exercise in its capacity as budgetary authority in its own right.

32. It is clear that this resource planning - like the triennial financial estimates themselves - can have no more than indicative value and be intended solely for the information of the budgetary authority.

---

1 Every year since 1976, the Commission has prepared a document entitled 'Comprehensive review of the Community's budget problems'. This document summarizes the economic and budgetary situation which is likely to prevail in the following financial year. It is submitted in April to a joint Council (Foreign and Finance Ministers). The document is also forwarded to the Parliament which may prepare a report but which does not discuss it directly with the Council

(b) Periodic review of the system of own resources

33. In the abovementioned proposal for the revision of Article 201, the Commission suggested including the following paragraph:

> 'At least every five years the Council, after receiving a report from the Commission and consulting the Assembly, shall examine whether and in what manner new resources should be created.'[1]

34. The working party should follow up this idea but interpret it more broadly. The review proposed by the Commission should take the form of a sort of general assessment of the current system of own resources, viewed from the point of view of its effectiveness and relevance to the present situation. This assessment should be made by the budgetary authority on the basis of a report drawn up by the Commission and, possibly, the Court of Auditors. It is essential that the Member States should be directly involved in this through specially appointed representatives. It would seem advisable therefore for the Community and national authorities to jointly review the general situation of Community finances every five years with a view to reaching at regular intervals some kind of general consensus on the future development and allocation of the financial costs implicit in further Community integration.

35. Any changes to the existing system which were felt to be necessary following this review could be introduced in accordance with the decision-making procedure described above.

CONCLUSIONS

36. After considering the various aspects of the decision-making machinery in the field of own resources the working party may reach the following conclusions:

(1) Removal of restrictions on the rate of Community VAT: Once the proportion of VAT reaches the 1% ceiling, the decision of 21 April 1970 should be amended to move any reference to ceilings. The Commission is asked to make the relevant proposals in due course.

(2) Changes to the decision-making process for the creation/alteration of own resources: Articles 200 and 201 of the Treaty should be updated stipulating agreement of European Parliament voting by qualified majority rather than ratification by the Member States for any decision to create or alter own resources. The Commission is asked to make appropriate proposals as soon as possible.

---

[1] See Annex II

(3) Planning and periodic review of the future pattern of own resources: The future pattern of own resources must be taken into account when the triennial financial estimates are being prepared and be considered jointly by the budgetary authority before the annual procedure for adopting the budget. Every five years the Community and national authorities should review the general system of own resources with a view to arriving at a consensus on the Community's financing needs, capacity and methods.

Annexes

FINANCIAL PROVISIONS OF THE EEC TREATY

Article 199

All items of revenue and expenditure of the Community, including those relating to the European Social Fund, shall be included in estimates to be drawn up for each financial year and shall be shown in the budget.

The revenue and expenditure shown in the budget shall be in balance

Article 200

1. The budget revenue shall include, irrespective of any other revenue, financial contributions of Member States on the following scale:

Belgium	7.9
Germany	28
France	28
Italy	28
Luxembourg	0.2
Netherlands	7.9

2. The financial contributions of Member States to cover the expenditure of the European Social Fund, however shall be determined on the following scale:

Belgium	8.8
Germany	32
France	32
Italy	20
Luxembourg	0.2
Netherlands	7

3. The scales may be modified by the Council, acting unanimously.

Article 201

The Commission shall examine the conditions under which the financial contributions of Member States provided for in Article 200 could be replaced by the Community's own resources, in particular by revenue accruing from the common customs tariff when it has been finally introduced.

To this end, the Commission shall submit proposals to the Council.

After consulting the Assembly on these proposals the Council may, acting unanimously, lay down the appropriate provisions, which it shall recommend to the Member States for adoption in accordance with their respective constitutional requirements.

ANNEX II

COMMISSION PROPOSAL (1973)

ON STRENGTHENING THE BUDGETARY POWERS OF PARLIAMENT

(Doc. 1000 final)

Article 201 of the Treaty establishing the European Economic Community to read:

'The Commission shall examine in what manner new resources may be allocated to the Communities.

At least every five years the Council, after receiving a report from the Commission and consulting the Assembly, shall examine whether and in what manner new resources should be created.

On a proposal from the Commission and after unanimous agreement in the Council, the Assembly, voting by a majority of its members and three-fifths of the votes cast, may change the existing ceiling on own resources or create new resources.'