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The EU Own Resources System – Reform Needs and Options

The most prominent and debated issues in the negotiations on the next Multiannual Financial Framework for the EU for the period 2014-2020 were the overall budget volume, the structure of expenditures and the continuation of the rebates for (some) net contributor countries. However, the system of the EU's own resources was hardly addressed in the negotiations, although it is one of the most important obstacles to reform. This article reviews the most important deficits of the current system of own resources and assesses the most substantial reform proposal which has been advocated for years by the European Commission, namely to finance part of the EU budget through EU taxes.

The negotiations on the next Multiannual Financial Framework (MFF) for the EU for the period 2014-2020 appeared to be even more conflict-ridden than those on the preceding four MFFs. The starting point of the negotiations was the European Commission's proposal, presented in June 2011, which envisaged for the whole seven-year period a total volume of commitment appropriations of €1,025 billion (in constant 2011 prices) or 1.05 per cent of EU27 gross national income (GNI). This proposal was updated in June 2012, primarily to account for the accession of Croatia in July 2013, to €1,045 billion (1.09 per cent of GNI). After several negotiation rounds and special EU summits, a compromise acceptable to the European Commission as well as the European Parliament could finally be reached in June 2013. A total volume of commitment appropriations of €960 billion (1.0 per cent of EU GNI) was agreed upon for the next MFF period. Thus, in relation to GNI, the volume of the next MFF falls markedly below the current one, which foresees commitment appropriations of 1.12 per cent of GNI for the period 2007-2013.

The most prominent and debated issues in the negotiations were the overall budget volume, the structure of expenditures and the continuation of the rebates for (some) net contributor countries. The need for fundamental reform of the composition of expenditures as well as the system of rebates is acknowledged in academia and to a large extent also in the EU institutions (European Commission, European Parliament, European Council). At the same time, however, this need for reform is ignored by many representatives of EU member countries in the European Council against the background of their country-specific interests in concrete negotiations.

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In contrast to the reform areas mentioned above, the system of the EU's own resources was hardly addressed in the negotiations, although it is one of the most important obstacles to reform. This is all the more remarkable as a fundamental redesign seems to be a central precondition for achieving a future-oriented EU budget from which individual member countries as well as the EU as a whole would benefit more than from the one just concluded.

EU expenditures: challenges and shortcomings[1]

Considering the increasing challenges the EU is facing – in particular recent and imminent enlargement rounds, structural problems of the southern peripheral countries, the financial and economic crises and its consequences (record youth unemployment, debt crisis in some highly indebted member states), and the increasingly pressing long-term challenges (climate change and energy transition, demographic change, increasing income and wealth inequality and risk of poverty) – the overall EU budget volume needs to be held constant, if not increased compared to the current MFF. The volume of the current MFF is already below the preceding one. Increasingly, the volume of the available funds will not be sufficient to keep up with the long-term increase of tasks and the corresponding financing needs.

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1 See for this section M. Schratzenstaller: Eckpunkte eines zukunftsfähigen EU-Budgets, OeGfE Policy Brief, Vienna 2013.

Table 1

Expenditure structure – MFF 2007-2013 and agreement on MFF 2014-2020

Commitment appropriations, in constant 2011 prices

	MFF 2007-2013		Proposal European Commission June 2012		Proposal Van Rompuy November 2012		Agreement Summit February 2013	
	In billion euros	In %	In billion euros	In %	In billion euros	In %	In billion euros	In %
Competitiveness and infrastructure	91.5	9.2	164.3	15.7	139.5	14.4	125.6	13.1
Cohesion policy	354.8	35.7	339	32.4	320.1	32.9	325.1	33.9
Sustainable growth: natural resources (CAP)	420.7	42.3	390	37.3	372.2	38.3	373.2	38.9
Security and citizenship	12.4	1.2	18.8	1.8	16.7	1.7	15.7	1.6
Global Europe	56.8	5.7	70	6.7	60.7	6.2	58.7	6.1
Administration	57.1	5.7	63.2	6.0	62.6	6.4	61.6	6.4
Compensation	0.9	0.0	0.003	0.0	0.003	0.0	0.003	0.0
Total	994.2	100.0	1,045.3	100.0	971.9	100.0	960	100.0
Total in % of GNI	1.12	-	1.08	-	1.01	-	1.0	-

Source: European Commission, own compilation.

Moreover, restructuring expenditures is required to support more effectively a more dynamic, inclusive and ecological growth and development path for the EU. Within the current MFF, the Common Agricultural Policy (CAP) and the Structural Funds together account for almost 80 per cent of total expenditures (see Table 1). The CAP (42 per cent of total expenditures) predominantly preserves existing (production) structures and pursues social goals (income support) within the so-called first pillar. Structural and cohesion policy (36 per cent of total expenditures) focuses too strongly on a traditional infrastructure policy favouring material (large-scale) infrastructure. As "richer" member countries benefit from subsidies within the CAP and cohesion policy to a substantial extent, funds are not redistributed to the "poorer" member states in a focused and targeted way. Less than ten per cent of the EU budget is dedicated to competitiveness (i.e. research and innovation) and infrastructure.

The new MFF for 2014-2020 dedicates 13 per cent of the total sum to competitiveness and infrastructure, 34 per cent to cohesion policy and another 39 per cent to agricultural policy, which implies only minor shifts in the current composition of expenditures. In contrast, strengthening the EU budget's role as an instrument to support a growth and development path that goes beyond the Europe 2020 strategy and is targeted more intensely on combining economic dynamics with ecological and social goals requires the following key elements:

- A stronger reduction of the expenditure share of the CAP, reinforcing the shift of agricultural expenditures to the second pillar of the CAP, which is based on ecological and employment goals;
- Reinforcement of the "greening" of direct payments within the first pillar of the CAP;
- A stronger focus by cohesion funds on "poorer" member countries and a corresponding reduction of funds for "richer" member countries;[2]
- Stronger coupling of cohesion funds with climate objectives and employment goals;
- A linking of cohesion funds with efforts to improve competitiveness and with the indicators applied within the EU's new economic governance (macroeconomic imbalances) to create a connection between the euro crisis and the EU budget;[3]
- A greater increase of the expenditure share for research and innovation, with a specific focus on ecological and social aspects.

2 K. Aiginger, P. Huber, M. Firgo: Policy Options for the Development of Peripheral Regions and Countries of Europe, WWWforEurope Policy Brief, No. 2, 2012.

3 P. Becker: Lost in Stagnation: Die Verhandlungen über den nächsten mehrjährigen Finanzrahmen der EU (2014-2020) und das Festhalten am Status quo, SWP-Studie, Berlin 2012.

Alternative revenue sources for the EU

Against the background of this (old) reform debate, some long-term trends concerning the level and composition of EU revenues and potential inherent problems are of immediate interest. It is therefore important to assess the most substantial reform proposal which has been advocated for years by the European Commission, namely to finance part of the EU budget through EU taxes.

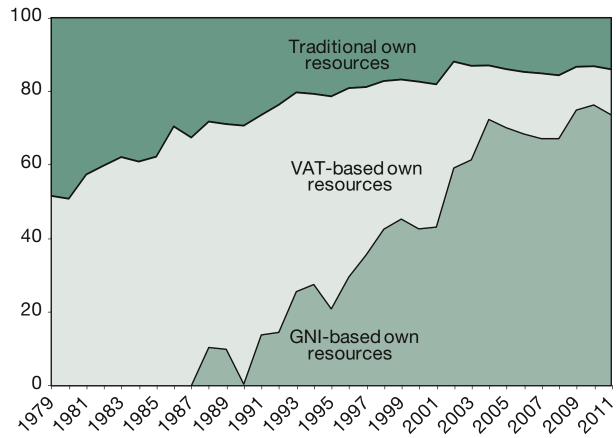
Volume and composition of EU revenues

The EU does not have the right to raise taxes or contributions in order to finance its own tasks. Rather, tax sovereignty within the EU is assigned to the member countries at the national level and – to a lower degree – at the sub-national level. A (very small) part of national tax revenues raised by member states is transferred to the EU. The EU currently has essentially three revenue sources: traditional own resources (agricultural tariffs, sugar customs duties, general tariffs), VAT-based own resources, and GNI-based own resources.[4] EU expenditures must be financed exclusively from own resources; the option of running a budget deficit is excluded by the EU Treaty.

The financing system of the EU has been changed six times through own resources decisions by the European Council and the European Parliament since 1970. Ad hoc national contributions by member states have been increasingly replaced by a system of own resources, and they vanished completely in 1982.[5] These own resources accrue to the EU directly, without any further decisions required at the national level. Total revenues are limited by the own resources ceiling.

Until 1980 the traditional own resources, introduced in 1968, were the EU's only financial source. They are collected by member states on behalf of the EU and directly transferred to the EU budget (minus a discount of 25 per cent, which remains with member states to cover the cost of revenue collection).[6] VAT-based own resources were introduced in 1979 as a residual financing source with a uniform call rate from a harmonised tax base

Figure 1
Composition of EU own resources
in %



Source: European Commission: Financial Report 2011, Brussels 2012.

which is limited to 50 per cent of national GNI (capping). At its introduction, the (maximum) call rate was fixed at one per cent; after being subsequently raised and reduced again in several steps, the call rate currently applied within the MFF 2007-2013 is 0.3 per cent. In the context of financing the "UK rebate", some net contributors have been granted a reduction of the call rate for the period 2007-2013 (Germany 0.15 per cent, Sweden and the Netherlands 0.1 per cent, Austria 0.225 per cent). The GNI-based own resource exists since 1988. As a residual financing source, it serves to balance the budget subject to the own resources ceiling; as a consequence, the call rates (which are identical for all member states) are updated each year.

Since the end of the 1970s, a remarkable structural shift can be observed in the composition of the EU's own resources (see Figure 1). Traditional own resources received directly by the EU have greatly diminished in importance. Whereas in 1980 they accounted for almost 50 per cent of total revenues, their share has since fallen steadily, declining to about 20 per cent in the mid-1990s and to about 15 per cent in 2005. Thus, the financing of the EU budget increasingly rests on direct contributions from member states' national budgets. The share of revenues from the VAT-based own resource reached its peak at 70 per cent in 1986 and 1990 before shrinking steadily thereafter to 12 per cent in 2011. In parallel, the share of revenues from the GNI-based own resource increased continuously from ten per cent in 1988 to 74 per cent in 2011.

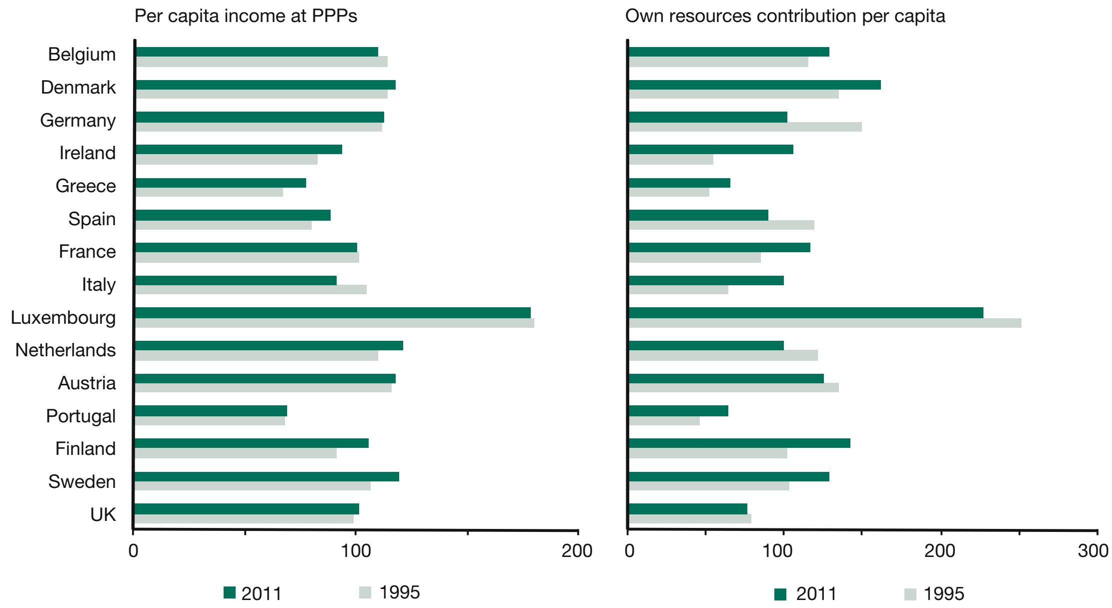
This development stems from two Council Decisions – from 1992 (effective as of 1995) and 1999 (effective as of

4 This revenue source was originally calculated on the basis of gross national product (GNP), but since 2002 it is determined on the basis of GNI (gross national income).

5 European Commission: Financing the EU Budget: Report on the Operation of the Own Resources System, Commission Staff Working Paper, SEC(2011) 876 final/2, Brussels 2011.

6 This flat-rate deduction was ten per cent until 2000. One of the European Commission's proposals for reforming the system of own resources is to reduce the rate from its current level of 25 per cent to the original level. See European Commission: Communication on the EU Budget Review, COM(2010) 700, Brussels 2010.

Figure 2
GNI and national contributions per capita
EU average = 100



Source: European Commission: Financial Report 2011, Brussels 2012, own calculations.

2002) – which have shifted the bulk of financing from the VAT-based towards the GNI-based own resource component. Part of this shift consists of the aforementioned cuts in the call rate for the VAT-based own resource to 0.3 per cent of the harmonised VAT base, which itself had been reduced to 50 per cent of national GNI over the same period. One motive for this move from VAT- towards GNI-based own resources was to widen the financial scope of the EU budget. Another was the easing of the financial burden on the economically weaker member states – while contributions on the basis of VAT are expected to have a tendentially regressive effect, the contributions linked to GNI better reflect a country's economic capacity.[7]

Whether this has actually aided the economically weaker member states cannot be examined and evaluated in detail here. However, the trend of GNI per capita is not necessarily parallel to that of national contributions per capita, as can be illustrated by the example of the 15 "old" member states (see Figure 2). For eight of these states, per capita incomes compared to the EU15 average moved in the opposite direction of their own resources contributions per capita in 2011 compared to 1995.

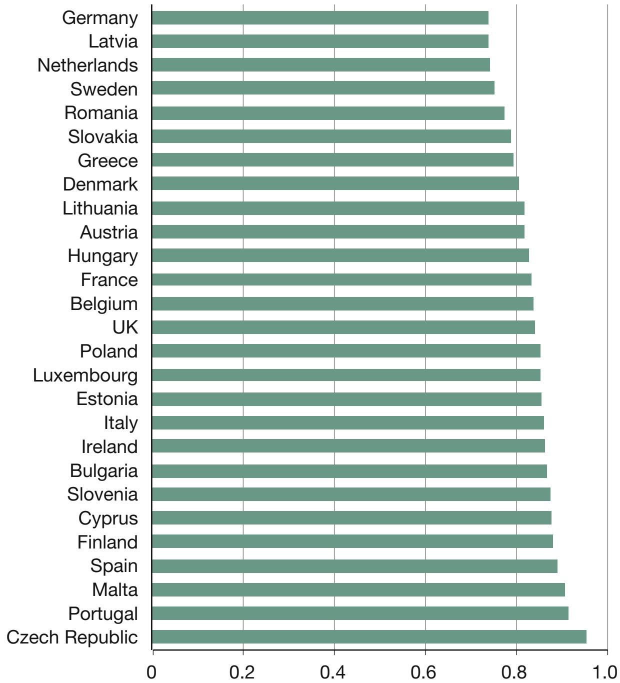
The gross contribution, i.e. total payments to the EU, is the most straightforward measure of a country's financial contribution to the EU budget. Deducting traditional own resources delivers the national contribution, consisting of VAT- and GNI-based own resources. The national contribution (see Figure 3) is more appropriate than the gross contribution for comparisons among member states, since it reflects the resources actually raised by individual member states. Figure 3 shows national contributions in per cent of GNI (including the UK rebate) for 2011. In 2011, the national contribution was lowest in Germany (0.74 per cent of GNI) and highest in the Czech Republic (0.95 per cent of GNI).

In the political debate and in EU budget negotiations, the net contribution position, as recorded in the national balance of payment statistics, plays a more important role than the national contribution. As the balance of financial transfers (VAT- and GNI-based own resources) paid to the EU and transfers received from the EU budget, it expresses a member state's financial net benefit or cost.

Since its introduction, the UK rebate – which amounted to €3.6 billion in 2011 – has been a topical issue in the context of the net contribution position. Following a decision of the European Council of Fontainebleau in 1984, the UK is reimbursed two-thirds of its annual net con-

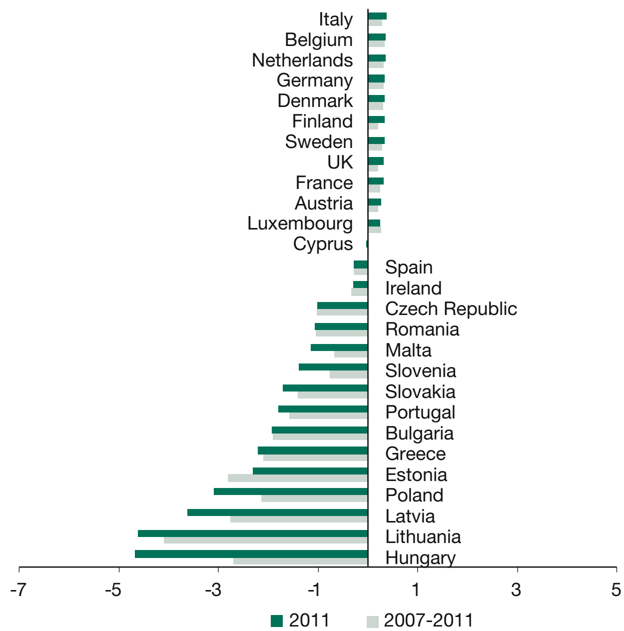
7 Deutsche Bundesbank: Neuere Tendenzen in den Finanzbeziehungen Germanys zur Europäischen Union, Frankfurt, 1999, pp. 59-74.

Figure 3
VAT- and GNI-based own resources, 2011
in % of GNI



Source: European Commission: Financial Report 2011, Brussels 2012.

Figure 4
Net contributions by member states
in % of GNI



Source: European Commission: Financial Report 2011, Brussels 2012, own calculations.

tribution. The special provision was successfully negotiated by former Prime Minister Margaret Thatcher at a time when the UK had a relatively low per capita income within the EU. Due to its comparatively small agricultural sector, the country received considerably less in EU agricultural payments than, for example, France. The adjustment in favour of the UK is financed by the other member states according to their levels of GNI. Since 2001, a special clause applies for the traditionally most significant net contributor countries Germany, Austria, Sweden and the Netherlands, which pay only 25 per cent of their normal financing share of the UK rebate.[8]

In 2011 as well as during the period 2007-2011, 11 of the 27 member states were net contributors.[9] In the period 2007-2011, the largest net contributors in relation to their GNI were Germany, Belgium, the Netherlands and Denmark (see Figure 4).

8 J. Clemens, A. Lemmer: Financing the EU Budget – Present Situation and Perspectives, CESifo DICE Report, Vol. 4, No. 1, 2006, pp. 39-44.

9 Cyprus's net position amounted to practically zero, with a net contribution of 0.02 per cent of GNI in the period 2007-2011 and of -0.04 per cent of GDP in 2011.

Problems and need for reform in the current system of own resources

The financing system of the EU is characterised by a number of shortcomings rooted in the low and still decreasing revenue autonomy of the EU.[10]

Increasing controversiality of size and structure of EU budget and dominance of national interests

Since the EU can neither raise its own taxes nor incur debt, its revenue autonomy has been limited from the outset. The EU's own resources consist primarily of member states' contributions paid directly from national budgets. Thus the EU budget has increasingly become the subject of political conflict, as most clearly revealed by the "net contributor debate". This carries the risk of the EU budget becoming chronically underfinanced for the challenges the EU will face in the future. This can be seen in the fact that both the current MFF and the one for

10 While the presentation of these shortcomings is structured somewhat differently, the aspects elaborated in this section are mainly those addressed in European Commission: Financing the EU Budget ..., op. cit. and several related academic studies cited therein.

the period 2014-2020 are on a declining path as a share of GNI.

The predominance of national contributions narrows the focus of member states to their monetary net returns from the EU budget, i.e. the relation between their contributions to the budget and the monetary returns from individual policy areas (common agricultural policy, structural and cohesion policy, research and innovation, etc.).[11] The benefits of EU membership beyond pure budget-related financial flows, however, do not play much of a role in the evaluation and decision criteria of member states.[12] Within the EU, with its increasing divergences and national interests, a perspective focusing on country-specific monetary costs and benefits inevitably aggravates the ongoing controversy over the EU budget and increasingly hinders compromises. It is a primary reason that particularly net contributor countries, whose gross contributions exceed transfers received from the EU budget, urge a limitation of the EU budget's volume. Moreover, it furthers the tendency of individual member states to support the preservation of those expenditure categories promising to maximise transfers that benefit them instead of pushing an expenditure structure from which a maximal benefit for the EU as a whole may be expected. The distributional conflicts as well as the "net contributor debate" have been aggravated by the various enlargement rounds and the (potential) burden from the EU rescue package, the largest part of which falls upon eurozone countries.

In this context, it should be recalled that the financial resources at the disposal of the EU also serve to finance various "European public goods", i.e. goods or activities with positive cross-border external effects[13] and with "European value added".[14] In particular, this concerns expenditures in the areas of research and innovation, education, transport infrastructure, and climate and energy policies decided upon at the EU level. Securing fiscal equivalence would also require assigning to the EU the taxes necessary to finance these expenditures.

11 European Commission, 2011, op. cit.; P. Becker, op. cit.

12 S. Richter: The EU's Multi-annual Financial Framework for 2014-2020: An Old Construct in a Changed EU?, FIW Policy Brief, No. 19, 2013.

13 In this context, consider the evolving debate about "global public goods"; see e.g. I. Kaul, I. Grunberg, M. Stern: Global Public Goods: International Cooperation in the 21st Century, New York-Oxford 1999.

14 European Commission: A Budget for Europe 2020: The Current System of Funding, the Challenges Ahead, the Results of Stakeholders Consultations and Different Options on the Main Horizontal and Sectoral Issues, Commission Staff Working Paper, SEC(2011) 868 final, Brussels 2011.

No contribution to EU policies

Moreover, the lack of tax autonomy at the EU level runs counter to the long-term trend of deepening economic integration. Despite an increase in negative cross-border externalities (e.g. environmental damage) caused by ever closer economic integration of member states, policy refrains, for example, from using taxes at the European level to influence economic agents' behaviour and thus foregoes potential benefits of a rather powerful market-based policy instrument. In general, the current revenue system hardly contributes or supports EU policies.[15]

Increasing complexitiy of the system of own resources and political legitimacy

The system of own resources is characterised by a considerable degree of complexity and lack of transparency. While the three revenue sources as such are easy to understand, their implementation is not. This is mainly caused by the UK rebate and the various mechanisms for its correction. In addition, the concrete design of the VAT-based own resource, particularly the determination of the tax base, is often criticised for being rather complicated.

Moreover, the structural adjustments made since the early days of the European Community are the result of political compromises (such as the correction mechanism for the financing of the UK rebate). Apart from the resulting administrative burden, this trend also undermines political credibility and support for national financial contributions, since the populations of the individual member states are less and less able to identify their own contributions to the financing of the EU budget and the relationship between revenue and expenditure.

Equality concerns

Within the group of net contributing countries, which in the period from 2007 to 2011 included 11 member states, a "rebate on the rebate" was granted only to those four countries which traditionally are the most significant net contributors, despite the fact that they do not necessarily carry the largest net contribution burdens in relative terms (see Figure 5). Therefore, the complete elimination of the correction mechanism for the UK rebate is an important element of a more simple, transparent and equitable system of financing the EU budget. This is all the more relevant, as the initial reason for granting a rebate to the UK – relatively low economic prosperity and high

15 European Commission: Financing the EU Budget … , op. cit.

net contributions – has disappeared during the last 30 years.[16]

From an equality perspective, it may also be considered problematic that poorer member states benefit from cohesion policy but, conversely, over-proportionately contribute to financing the various correction mechanisms to alleviate the net contribution burden of the richer countries.[17] It may also be criticised that capping individual VAT-based resource payments by limiting the portion of the harmonised VAT base on which the call rate is applied to 50 per cent of GNI does not necessarily alleviate the burden for the poorer countries, as there is no clear relationship between a country's GNI and the size of its VAT base.

Options for a fundamental reform of the system of own resources of the European Union

Current state of the political discussion

The MFF 2007-2013 has not brought about any fundamental changes for the system of own resources. In its proposal for the own resources decision (part of the whole package related to the MFF 2014-2020), the European Commission suggested three elements of reform to the current system of own resources:[18] firstly, the simplification of member states' contributions by eliminating the VAT-based own resource; secondly, the introduction of new own resources (preferably a financial transaction tax and a new VAT resource); and thirdly, the reform of correction mechanisms through implementation of a new system of lump sum payments to replace all pre-existing correction mechanisms.

The European Parliament has for the first time exercised its power, introduced by the Lisbon Treaty, to legislate in co-decision with the Council on the MFF, rejecting the Council's MFF agreement from February 2013 in its resolution of March 2013 before finally accepting it in June 2013. The European Parliament has been demanding for some time now a reform of the system of own resources, including the reform of the existing VAT-based own resource and the introduction of an EU tax, i.e. a genuine own resource (particulary a financial transaction tax). Up to now, the European Council has refused to negotiate on the reform of the system of own resources and on the introduction of an EU tax in particular.

Central elements of a reform of the system of own resources[19]

Options for the reform of the EU system of own resources have been considered for some time at the EU level. Following up on agreements reached in the context of the last few financial frameworks, the European Commission has submitted several reports on the functioning of the system of own resources,[20] most recently in 2011.[21] These documents also discuss the pros and cons of various financing alternatives. In principle, two alternative reform strategies to address the existing shortcomings of the system of own resources may be envisaged:[22]

- Reforms within the existing system of own resources with the aim of streamlining it. In practice, this would lead to the elimination of the VAT-based own resource so that, given the ongoing loss in importance of traditional own resources, the budget would in the long run be financed almost entirely by GNI-based own resources.
- Introduction of dedicated EU taxes as a (partial) compensation for the existing revenue sources. This option, favoured by the European Commission, would assign some degree of tax autonomy to the EU.

The criticism advanced against the current system of own resources advises in favour of the latter reform strategy, conferring to the EU some degree of tax autonomy in combination with a reform of key features of the existing system of own resources along the following lines:[23]

- elimination of VAT-based own resources;

16 Ibid.
17 Ibid.
18 European Commission: Proposal for a Council Decision on the System of own Resources of the European Union, COM 2011(510) final, Brussels 2011; European Commission: Amended Proposal for a Council Decision on the System of own Resources of the European Union, COM 2011(739) final, Brussels 2011.

19 The following sections draw heavily on M. Schratzenstaller, B. Berghuber: Alternative Financing Sources for the EU Budget, in: Austrian Economic Quarterly, Vol. 12, No. 1, 2007, pp. 34-50.
20 European Commission: Financing the European Union, Commission Report on the Operation of the Own Resources System, Brussels 1998; European Commission: Financing the European Union, Commission Report on the Operation of the Own Resources System, COM(2004)505, Brussels 2004.
21 European Commission: Financing the EU Budget … , op. cit.
22 European Commission: Financing the European Union … , 2004, op. cit.
23 These key features are also mentioned by the European Commission, which nevertheless pleads in favour of the revenue-neutral introduction of a new own revenue source which should cover up to 50 per cent of total expenditure. See European Commission: Financing the European Union … , 2004, op. cit.

- introduction of EU taxes to compensate for the abolition of VAT-based own resources and in recognition of the arguments in favour of EU tax autonomy;

- reinforcement of EU tax revenues through GNI-based own resources;

- reform of the correction mechanism to finance the UK rebate.

Evaluation of potential EU taxes as a central pillar of a fundamental reform of the system of own resources

Starting from these key elements, the following considerations are devoted to a crucial aspect in the debate on alternative revenue sources for the EU budget, i.e. the question of what kind of taxes would lend themselves as EU taxes.[24] One basic assumption here is that financing the EU budget entirely or at least primarily through EU taxes is for the time being neither meaningful nor possible under the existing framework conditions. One argument against is the existing ban on incurring debt, which requires an additional revenue source to balance the budget in case actual tax revenues fall short of projections. In addition, financing all EU responsibilities entirely by EU taxes would require much deeper political integration among EU member states than is presently the case, leading more towards a federal state.

Weighing the pros and cons of EU taxes on the one hand and GNI-based own resources on the other is an issue beyond pure economic reasoning. Rather, it is a political question for member states to determine whether they see the Union eventually evolving towards a federal state that in the end needs its own legal framework for fiscal relations and tax sovereignty. This is also a crucial factor for the degree and factual implementation of the tax autonomy conferred to the EU:[25] it may either be confined to the power to decide on how to allocate its own resources, or it may extend to legislative powers in tax matters. In the first case, the EU would receive a certain fraction of national tax revenues or be granted the right to levy a supplementary rate on a given tax base, with the right to decide on tax bases and national tax rates essentially remaining with the member states. In the second case, the EU would acquire the right to determine the tax base and rate, with member states possibly having the right to levy a supplement.

In its reports on the operation of the EU own resources system, the European Commission establishes seven criteria for the evaluation of own resources:[26]

- visibility and simplicity
- financial autonomy
- contribution towards an efficient allocation of economic resources
- yield
- cost efficiency with regard to tax administration
- revenue stability
- equitable gross burden.

These criteria may be applied only partially or in modified form in the following assessment of the suitability of different taxes as financial sources for the EU budget. They will be supplemented by further criteria developed within the theory of fiscal federalism as a yardstick for assigning different taxes to the different levels of government.[27] Thus, for the assessment of whether a certain tax may qualify as an EU tax, the following criteria may be formulated:[28]

- Degree of regional attribution: the lower the possibility to determine the share of individual member states in the tax base/tax revenues, or the lower the identity between the country where tax revenues accrue and the country of residence of tax subjects, the higher the suitability as an EU tax.

- Cross-border negative externalities: the higher these are, the higher the qualification as EU tax, since the optimal tax rate from the national perspective is below the one from the European perspective.

- Mobility of the tax base: the higher it is, the higher (in principle) the qualification as an EU tax, since centralisation may help to prevent a possibly harmful “race to the bottom”.

- Short-term volatility: the higher it is, the lower the qualification as EU tax. Due to the ban on EU debt,

24 See also S. Richter: In Search of New Ways for Financing the Budget of the European Union, presentation at WIIW, Vienna 2006.

25 For elaboration on this point, see P. Becker: Der EU-Finanzrahmen 2007-2013, SWP-Studie, Berlin 2005, p. 36.

26 European Commission: Financing the European Union …, 2004, op. cit.

27 See e.g. R.A. Musgrave: Who should tax, where and what?, in: C.E. McLure (ed.): Tax Assignment in Federal Countries, Canberra 1983; R.H. Gordon: An Optimal Taxation Approach to Fiscal Federalism, in: Quarterly Journal of Economics, Vol. 98, No. 4, 1983, pp. 567-568; R.P. Inman, D. Rubinfeld: Designing Tax Policy in Federalist Economies: An Overview, in: Journal of Public Economics, Vol. 60, No. 3, 1996, pp. 307-334; C.E. McLure: The Tax Assignment Problem: Ruminations on How Theory and Practice Depend on History, in: National Tax Journal, Vol. 54, No. 2, 2001, pp. 339-363.

28 See also European Commission: Financing the European Union …, 1998, op. cit.; European Commission: Financing the European Union …, 2004, op. cit.

the flow of own resources should be stable in the short term and as cyclically insensitive as possible.

- Long-term yield (revenue elasticity): the higher it is, the higher the qualification as an EU tax. European integration and the long-term challenges facing the EU will require a wider range of tasks, and therefore the financial needs will probably rise.

- Visibility: the more visible and perceptible a tax for the taxpayer, the higher its qualification as an EU tax, since the link between tax payment and return from the EU budget is thus made transparent.

- Equality of gross burden at the national level: the closer the link between the tax base (and therefore the tax burden) and national income, the higher the qualification as an EU tax.

Table 2 gives an overview of the candidates for new own resources mentioned in the European Commission's various reports on the functioning of the system of own resources and options for its reform. Table 3 contains key features and potential revenues of the candidates (except for revenues from auctioning under the greenhouse gas Emissions Trading System) included in the European Commission's latest documents on the operation of the system of own resources and options for its reform. Altogether, the potential revenues of the various candidates may significantly contribute to financing the EU budget.

Table 2
Candidates for new own resources

European Commission (1998)	European Commission (2004)	European Commission (2010)
CO_2 or energy tax	EU energy tax	taxes on the financial sector (financial transaction tax and financial activity tax)
modified value added tax	EU value added tax	revenues form auctioning under the greenhouse gas Emissions Trading System
excises on tobacco, alcohol and mineral oil	EU corporate income tax	charge related to air transport
EU corporate income tax		EU VAT
tax on transport and telecommunication services		EU energy tax
income tax; interest income tax		EU corporate income tax
tax on ECB gains from seignorage		

Source: Own compilation based on European Commission: Financing the European Union, Commission Report on the Operation of the Own Resources System, Brussels 1998; European Commission: Financing the European Union, Commission Report on the Operation of the Own Resources System, COM(2004)505, Brussels 2004; European Commission: Communication on the EU Budget Review, COM(2010) 700, Brussels 2010.

Most revenue could be created by introducing a general *Financial Transaction Tax* (FTT) of 0.1 per cent on transactions of bonds, shares, and currency and of 0.01 per cent on transactions of derivatives. According to a conservative estimate by the European Commission, the potential yield may reach about €50 billion per year by 2020, which would cover about a third of the EU's annual expenditures according to the European Council's agreement of February 2013. In a version exempting currency transactions, the FTT would still raise about €20 billion or 15 per cent of the EU expenditures.

A *Financial Activities Tax* (FAT) of five per cent on the sum of profits and remuneration of financial institutions, as an alternative tax on the financial sector, is expected to yield about €25 billion per year and could thus finance about 18 per cent of the EU expenditures.

Revenues from charges related to air transport (a *Departure Tax* or *Flight Duty Tax*) and from an EU *Value Added Tax* (VAT) of one per cent on the goods and services subject to the standard tax rate are each estimated to raise about €20 billion per year (15 per cent of the EU expenditures).

An EU *corporate income tax* (CIT) of less than two per cent on the national corporate income tax base may yield about €15 billion (11 per cent of the EU expenditures).

The evaluation of these taxes according to the criteria specified above (provided in Table 4) gives only rough indications, since it does not allow for a possible fine-tuning of the different criteria but only distinguishes between "rather suitable" or "rather less suitable" as an EU tax. For further considerations on the actual design of an own resources system which is based on EU taxes as genuine own resources, the analysis of course needs to be refined. It would also have to consider administrative costs and the question of whether revenues would be collected at the national or EU level. None of the taxes briefly discussed here can be deemed an "optimal" EU tax, since all of them fail to fulfil at least one of the criteria defined above.

Table 3
Potential EU taxes

Tax base (tax)	Key features	Potential revenues per year	% of EU expenditures per year[1]
Financial transactions (Financial Transaction Tax)	0.1% tax rate on transactions of bonds and shares, 0.01% tax rate on transactions of derivatives	€ 20 billion (by 2020)	15
	0.1% tax rate on transactions of bonds, shares and foreign currency, 0.01% tax rate on transactions of derivatives	€ 50 billion (by 2020)	36
Sum of profit and remuneration of financial institutions (Financial Activities Tax)	5% tax rate on sum of profit and remuneration of financial institutions according to the addition-method FAT applied at source No fully harmonised tax centrally collected at EU level, but revenue-sharing between member states and EU	€ 24.6 billion (2009)	18
Charge related to air transport (Departure Tax or Flight Duty Tax)	Tax on passengers flying from an EU airport, differentiated according to distance and class of travel (Departure Tax) Tax on flights (Flight Duty Tax) Decentralised or centralised collection possible	€ 20 billion (by 2020)	15
Consumption (EU Value Added Tax)	1% tax rate on goods and services subject to standard tax rate Decentralised collection and transfer to EU	€ 20.9 billion to € 50.4 billion (2009)	15
Energy consumption CO_2 emissions (EU Energy Levy, EU CO_2 Levy)	Single EU tax rate on quantities of energy products released for consumption based on their energy content Minimum rate of CO_2-related taxation defined in revised ETD Decentralised or centralised collection possible	No estimates available	-
Profits of incorporated firms (EU Corporate Income Tax)	Less than 2% tax rate on national corporate income tax base Decentralised collection and transfer to EU	€ 15 billion	11

[1] Expenditures per year calculated as average of total expenditures for the period 2014-2020.

Sources: European Commission: Communication on the EU Budget Review, COM(2010) 700, Brussels 2010; European Commission: Financing the EU Budget: Report on the Operation of the Own Resources System, Commission Staff Working Paper, SEC(2011) 876 final/2, Brussels 2011; European Commission: Proposal for a Council Decision on the System of own Resources of the European Union, COM 2011(510) final, Brussels 2011; own compilation.

According to these criteria, charges on air transport would best qualify as EU taxes. They may internalise negative cross-border externalities (in this case, climate-damaging emissions) and thereby reduce air traffic. Assigning these taxes to the EU would rein in the possibility of tax avoidance caused by tax rate differentials between member states. Their visibility for citizens as well as short- and long-term revenue stability and tax yield are further arguments in favour of assigning them to the EU level. In particular, the tax avoidance to be expected speaks in favour of earmarking charges related to air transport entirely for the EU – a uniform tax rate should be fixed at the EU level and all revenues channelled into the EU budget.

The main arguments in favour of assigning an FTT to the EU as an own tax are the impossibility of a regional attribution of such a tax and its prospective long-term yield. Moreover, unilateral implementation would be next to impossible, and considering the far-reaching integration of the European financial market, the FTT may also internalise negative cross-border externalities. In contrast to an EU CIT or VAT, differing national tax bases would not be an issue.

An argument in favour of a partially centralised CIT is that the growing disconnect between value added and corporate location, on the one hand, and profit and its taxation, on the other, undermines the possibility of regional attribution of the tax. Moreover, it can be expected that corporate tax competition in the EU will intensify further due to the high mobility of the tax base. The CIT is also characterised by a high yield in the longer term.

Taxes on energy consumption have the advantage of low short-term volatility and high long-term elasticity. Moreover, they can internalise cross-border externalities and are highly visible to citizens.

The VAT appears to be the least suitable candidate. Only its long-term revenue elasticity and high visibility for citizens speak in its favour.

Altogether the most straightforward option for an EU tax is the FTT, which as a new tax has the additional advantage that national revenues would not be affected, which would be the case for charges on air transport and energy taxes, which exist at least in some member states already. Thus, it can be expected that choosing the FTT

Table 4

Evaluation of options for EU taxes

	Regional attribution	Negative cross-border externalities	Mobility of tax base	Short-term volatility	Long-term yield (revenue elasticity)	Visibility	Equality of gross burden at national level
Financial Transaction Tax	+	+	+	-	+	-	-
Financial Activities Tax	+	+	+	-	+	-	-
Departure/Flight Duty Tax	-	+	+	+	+	+	-
Value Added Tax	-	-	-	-	+	+	?
Energy Levy/CO_2 Levy	-	+	-	+	+	+	?
Corporate Income Tax	+	-	+	-	+	-	-

Note: + speaks rather in favour of being used as an EU tax; - speaks rather against being used as an EU tax.

Source: Own compilation.

as an EU tax would meet less political resistance than options which imply redirecting national revenues to the EU budget.

From an administrative point of view, the FTT has the further advantage that there are no nationally differing tax bases that would need to be harmonised beforehand. It could cover a substantial share of total EU expenditures by itself, but if the aim is to extend the contribution of EU taxes even further, charges related to air transport would be another readily available solution, considering that only a few member states currently levy such charges and that they are exposed to frequent criticism, as they are regarded as a severe competitive disadvantage when implemented unilaterally at the national level.[29] The same holds for a CO_2 tax, which some member states have introduced rather recently.

When designing a new financial framework for the EU that will offer a certain degree of tax autonomy, including institutional aspects and political decision-making processes, a number of caveats need to be considered that are often emphasised by the opponents of EU taxes. A major concern is that an own tax responsibility of the EU would lead to permanent upward pressure on expenditures, all the more so as the EU budget is dominated by the goal of redistribution. Moreover, the assignment of (a certain degree of) tax autonomy to the EU would require the reinforcement of its democratic legitimacy, i.e. via a further strengthening of the powers of the European Parliament as well as a tightening of expenditure control and the fight against fraud. It can also be expected that the process of unwinding the UK rebate system will cause considerable political controversy. Therefore, any major reform is likely to require a considerable lead time. In this context, the problematic role of the unanimity rule as a major barrier to far-reaching reforms needs to be emphasised. It is one of the main reasons that member states prefer to agree on a minimum consensus and for their principally critical attitude towards ambitious reform proposals.[30] By restricting themselves to incremental changes, member states avoid the risk of not reaching a final agreement.

Conclusions

There are many good reasons to substitute a substantial share of the existing own resources financing the EU budget with EU taxes. Most remarkably, many proponents of a fundamental future-oriented reform of EU budget expenditure structures, who form the overwhelming majority among experts and politicians, appear thus far not to realise that the current system of own resources is one of – if not the – most influential causes of the existing shortcomings of the expenditure side of the EU budget. Among other advantages, these EU taxes, which help to internalise negative externalities, would enable a reduction of the national contributions financed by more distorting taxes levied by member states. Thus, the introduction of such EU taxes may also contribute to current efforts to improve the structures of national tax systems.

29 Austria therefore has just reduced the rates of its flight charge, which was introduced in 2011 as one consolidation measure.

30 P. Becker: Lost in Stagnation: Die Verhandlungen über den nächsten mehrjährigen Finanzrahmen der EU (2014-2020) und das Festhalten am Status quo, SWP-Studie, Berlin 2012.