Strengths and Weaknesses of the EU Own Resources in Light of the Alternatives

Dr. Michael Thöne
Managing Director & CEO, FiFo Köln

Presented at the Workshop
„Reform Options for EU Finances put to test“
Federal Ministry of Finance, 14 June 2017, Berlin
Strengths and Weaknesses of the EU Own Resources in Light of the Alternatives

I. EU BUDGET AT A GLANCE
Composition of EU Revenues and Spending

EU Revenue (2015): € 146.03 billion

- GNI-based own resource 69%
- VAT-based own resource 12%
- Traditional own resources (TOR) 13%
- Surplus from previous year 1%
- Other revenue 5%

EU Expenditure (2015): € 145.24 billion

- Sustainable Growth: Natural Resources (i.e. Agriculture) 39%
- Economic, social and territorial cohesion 35%
- Global Europe and outside EU 11%
- Competitiveness for growth and jobs 9%
- Administration 5%
- Security and Citizenship 1%

Source: Own Calculations; based on COM-Data.
Core characteristics of the system

**Multiannual Financial Framework (MFF 2014-2020)**
with dual spending ceilings for each annual budget.

Majority of spending is fixed; some new **flexibility** instruments have been established.

MFF-approval entails acceptance of **maximum annual revenue ceiling** (1.2 % of GNI).

Actual Own Resources are financed **automatically**, increased and decreased according to expenditure needs.

Therefore, **deficits and debt** are impossible.

OR appear only in national budgets, not in view of the European citizens.
Strengths and Weaknesses of the EU Own Resources in Light of the Alternatives

II. SYSTEMIC BENCHMARKS
What are strengths and weaknesses?

“Everybody agrees that the current system is too opaque, too complex and, let's be frank, outdated. However, unanimous agreement on the need to improve the current system is one thing, finding a fairer, more transparent and more modern system likely to be agreed by all is another thing.” (Former EU Budget Commissioner Janusz Lewandowski on the occasion of the first HLGOR meeting, 4 April 2014).

Is 

unanimity  

really the  

dominant  

obstacle? 

And does really  
everybody 
agree?

Remember:  
The grass is always greener on the other side of the fence.

Suggestive solution:  
Current OR and its alternatives are evaluated on a equal footing using identical criteria.

Indeed?  
Whether a certain feature of a revenue source is considered a strength or a weakness depends i.a. on the assigned function of the instrument.

Own resources were designed to replace Member States’ financial contributions, not taxes. Both have different systemic benchmarks.
Future of Europe: 5 Scenarios and their financing

- Confederation: Non-increasing, mainly delegated powers. Revenue: Transfer-type OR.

Scenario 1: "Carrying on"
Scenario 2: "Nothing but the single market"
Scenario 3: "Those who want more do more"
Scenario 4: "Doing less more efficiently"
Scenario 5: "Doing much more together"
Treat different things differently

• The current OR system is dominated by an intergovernmental fiscal-equalisation logic. (Exception: TOR)
• Most of the options for new resources are dominated by an interpersonal tax logic.
• It is not impossible to combine both systems. But we should be aware of the differences, especially of the different functions of both systems.

• Thus, two different questions arise:
  1. What are the strengths and weaknesses of the transfer-type OR? How can this system be improved?
  2. How strong is the case for European taxation? Does successful harmonisation necessitate an European revenue authority?

• (This presentation concentrates primarily on the first question.)
Strengths and Weaknesses of the EU Own Resources in Light of the Alternatives

III. STRENGTHS AND WEAKNESSES
Strengths of the current OR (within the MFF system)

- Budgets are always balanced; EU deficits and surpluses are impossible.
- Budget discipline is ensured by the MFF.
- Revenues for the Union are predictable and reliable (in the mid-term).
- Easy and timely adoption of annual budget.
- MS’ contributions are quite fair and proportional to GNI (see next slide).
- Majority of the OR, i.e. GNI-OR and TOR, are simple and transparent.
- Financing via OR is a (necessarily small) stabiliser in economic crises.
Fairness: Correlation of Total OR and GNI (2015)

- Regularly, a very close correlation.
- Fun fact: Total OR and GNI are correlated even closer than GNI-based OR and GNI. ($R^2 = 99.4\%$)
- Surprising (but only true in 2015).
- Financing of EU: Almost immaculate proportional financing rate
- Based on a straightforward (& simple) ability-to-pay principle applied to MS

Source: Own Calculations; based on COM-Data.
## Weaknesses of current OR

<table>
<thead>
<tr>
<th>Problem / Criticism</th>
<th>Solve within system?</th>
<th>Tax a potential remedy?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statistical VAT-based OR complex and non-transparent</td>
<td>Reform VAT-OR; or increase GNI-OR</td>
<td>Possible. Transparency depends on design</td>
</tr>
<tr>
<td>Rebates (and rebates from financing the rebates) are unfair, complex and non-transparent</td>
<td>Abolish (use BREXIT)</td>
<td>Rebates also plague tax harmonisation</td>
</tr>
<tr>
<td>Delayed payments, ‘reste à liquider’</td>
<td>Making available-regulation etc.</td>
<td>Reliability of tax revenue?</td>
</tr>
<tr>
<td>Presentation of OR in national budgets heterogeneous and misleading</td>
<td>Harmonise presentation</td>
<td>Tax revenues disappear from national budgets</td>
</tr>
<tr>
<td>“Juste retour”-thinking on the national level</td>
<td>Not conceivable</td>
<td>Tax decreases this transparency</td>
</tr>
<tr>
<td>Limited margin of manoeuvre for new priorities</td>
<td>Feature of MFF</td>
<td>Feature of MFF</td>
</tr>
<tr>
<td>Missing accountability-link to voters</td>
<td>Not feasible</td>
<td>Feasible (but probable?)</td>
</tr>
<tr>
<td>EU added value: Decrease harmful tax competition</td>
<td>Not feasible</td>
<td>Harmonisation? …</td>
</tr>
<tr>
<td>EU added value: Use taxation for regulation</td>
<td>Not feasible</td>
<td>… or centralisation?</td>
</tr>
</tbody>
</table>
Three Dimensions of OR Reform

Current OR-system: If it’s not broken don’t fix it
- Within the realm of current EU, current system is “okay”.
- Operational improvements beneficial — and feasible.
- Day-to-day processes may be sometimes frustrating — as with all revenue systems.

How strong is the case for European taxation today?
- Does successful harmonisation necessitate a European revenue authority?
- If yes, the revenue should be used to unburden the standard OR.

Growth and deepening of the Union
- US-type federation makes a strong case for Euro taxes.
- Deeper cooperative federation will need a transfer-tax-mix beyond the MFF.
Thank you

Continuing the dialogue:

thoene@fifo-koeln.de

wwwfifo-koeln.de
Sources

Note: This a standalone presentation. It is original work, not based on a background paper or report. Naturally, the arguments benefitted strongly from the sources quoted.

- Cipriani, G. (2014), Financing the EU Budget, CEPS, Brussels.
- High Level Group on Own Resources (2016), Future Financing of the EU; Final report, Brussels, Dec 2016.