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The system of own resources in the European Union in the perspective of Eastern Enlargement

Abstract

The system of own resources was introduced in 1971 to give the Community some financial autonomy from member states' transfers and to support supranational method of integration. Then, due to the lack of clear *finalité politique*, it was shaped by politicians according to current needs of public finances and to decision-making procedures in the Community. Therefore it became somewhat inconsistent with basic ideas written in the Treaties and deeper reforms are expected. It is not evident, however, which way they will go because opinions of the Commission and of the European Council vary on this subject. The re-evaluation of the system (in 2005 at the latest) will undoubtedly take into account the implications of the next enlargement. It is arguable that the new member states should take part in shaping the new solutions. Their accession will make inadequate the financing provided by own resources and will reopen discussion on equity of the system among old members. The system will become more difficult to control because public authorities in new member states will not have enough experience in handling the revenues owed to the EU. Bigger financial revenues, combined with non-transparent procedures, will make the system less cost effective. It seems that granting more financial autonomy to the system might be crucial for its reform.

1. Main features of the general budget of the European Union

The public finances of the EU consist of three main elements. The general budget, which plays the most important role in the system, serves to finance the policies of the European Community, of the European Atomic Energy Community as well as the administrative expenditures of the EU institutions. The operating budget provides funds for the European Coal and Steel Community. The European Development Fund helps the less developed ACP countries co-operating with the EU, in the framework of the Lomé Conventions. The activities of the European Investment Bank and the lending and borrowing operations the European Commission in the international financial markets, being of relatively minor importance, complement these 3 sources of money needed to implement the EU policies.

The budgetary framework is based on articles 268 – 280 of the Treaty establishing the European Community. Six major principles[1] resulting from the EU legislation determine the scope of possible reforms of the system as well as the budgetary policies, which are reflected in the structure of expenditures and revenues. The principles provide for:

1. Unity, meaning that all the Union's revenue and expenditure must be brought together in a single budget.
2. Universality, meaning that revenue may not be assigned to particular expenditure and that all revenues and expenditures are entered in full into the budget without any adjustment against each other.
3. Annuality, meaning that expenditures equal revenues in each financial year (with the provisions for funds and payments covering multiannual operations).
4. Equilibrium, meaning that the budget is balanced and the estimated revenues for a given year equal the estimated payments. As a result, there is no budget deficit or surplus.
5. Specification of expenditure, meaning that each spending must be assigned to the specific objective making the budget unambiguous and transparent.
6. Neutrality, meaning that the budget was never prepared in any of national currencies but in a special unit of account or in a common currency (which since 1999 has been euro).

These principles are decisive for understanding the specific character of the EU public finances. Their role is more evident when one refers either to a budget of an international organisation or to a budget of a sovereign state. The first approach would in a sense minimise political, economic and social dimension of European integration: in fact the European Union regime is definitely much more complex than any other "policy regimes", like the United

[1] *The Community budget: the facts in figures*, 2000 edition. Office for Official Publications of the European Communities, Luxembourg 2000 p. 6. The principles reflect certain guidelines and should not be taken too literally, for example the balance rarely equals zero but the surplus (or deficit) is included into the next year budget correcting it respectively.

Nations, the World Trade Organisation, the North Atlantic Treaty Organisation etc. The better method is therefore to explain the role of the Union budget using the context of a market economy in a democratic state.

The EU general budget is an important tool of common public finances. In spite of this formal analogy to a national budget, it has certain features, which are the reason why any direct similarities between the two may be misleading. This is true both in budgetary policy and in budgetary system.

First of all, a national budget reflects economic potential of a country and directions of its policies. Bigger countries can afford bigger budgets and therefore their governments usually have more to say in international arena. The size of a budget in relation to GDP illustrates the degree of state intervention in the economy. The structure of a budget shows how protective the state is towards its citizens, indicates whether the government favours economic growth or current consumption and informs how freely the market system operates. The balance of a budget is considered an important indicator of internal equilibrium in the domestic economy reflecting the role of demand-oriented policies in stimulating its short-term performance.

It would be a futile task to look for all this information in the budget of the European Union. In 1999 its expenditure constituted only less than 1,3 per cent of the combined GDP in member states and about 2,5 per cent of their public spending The share of federal expenditure in the GDP of the USA is over 20 per cent. Therefore the US federal government can afford a deficit being even several times bigger than the total EU budget expenditure! Such a small budget, however, does not prevent the EU from being one of the three major players in the world economy and from ensuring high quality of life to its citizens. There are several reasons for this apparent incoherence. First, the most expensive public policies (social security, defence, education, internal security) are financed mainly from member states' budgets and not from common money. Second, many common policies are functional by nature and do not require much funding except for administrative costs of introducing and implementing the legislation (trade, competition, transportation). Third, the principle of subsidiarity means that the EU covers the costs of economic integration together with national and regional governments as well as with businesses, which partly pay the burden of implementing various standards stemming from the evolving single market. Four, the expenditure of the EU budget has been strongly concentrated. It provided significant resources for agriculture and structural policies in order to keep the differentiation of incomes within the limits acceptable for all member states. For finances of some of them the role of transfers from Brussels was well beyond than the low average share of common budget in common GDP would suggest.

This unique approach to the EU public policies means that the functions of its budget have been more limited than the traditional functions of national budgets. Assigning 80 per cent of expenditure to agriculture and structural policies, the EU budget actually fulfils mostly the redistributive function. All member states consider its funds as important, especially the net beneficiaries and the net contributors which actively bargain over the value and structure of revenue and payments. The allocative role of the EU budget has been of minor importance – it supports education, training, the internal market, research and technological development. These areas are in principle financed from national resources and the role of common funding is not decisive for their development. Similarly, the stabilising function practically has not materialised yet. There are no fiscal transfers provided to soothe economic disturbances in various regions of the single market. Subsequently, although the expenditure may exceed the income (and vice versa) in a given year, the resulting balance has a technical character. It cannot be financed with the debt issued by the EU institutions. In accounting and economic terms the budget has to be balanced and therefore it is not a tool to quickly face the unforeseen events.

The budget-sharing method of integrating public finances has also important political consequences. First of all, keeping the Union's budget low, the member states limit ceding their sovereignty to the common pool and limit the role of supranational institutions in integration. On the contrary, it still predominantly depends on intergovernmental co-operation and financing through national budgets. The member states exercise additional control over community money at the administrative level.[2] As a result, the EU activities in many areas have limited effects due to the difficulties in mobilising necessary resources or simply to the waste of them. Such a situation contributes to the fact that the EU is neither breaking paths in technological progress and is not a leader in a "new economy", nor it is able to guarantee peace even in European continent. Both factors may put in doubt its aspirations to be a global player in a world policy and economy.

[2] "The implementation of the EU budget is characterised by a fragmentation of responsibilities between the Commission and public authorities in the member states (....) 80 % of the budget is managed on behalf of the EU by the member states." B. Lafan and M. Shackleton – *The Budget,* in: H. Wallace and W. Wallace (eds)– *Policy making in the European Union,* 4th edition, Oxford University Press 2000 p. 226.

2. The elements of the system of own resources

As it was already mentioned, the general budget is the most important part of the EU public finances. Its revenue side is called the system of own resources. It is a less known part of the EU budget probably not only in Poland. Most textbooks and monographs on European integration refer extensively to the expenditure side of the budget, usually when the authors discuss relevant common policies using majority of payments: agriculture and regional. The media coverage of budgetary issues is especially biased: the public opinion is informed about the amount of financial flows Poland can expect before and after accession, being silent on where the EU budget money come from as well as on what will be Poland's contribution to Community finances. It is fair to assume that not many Poles expect that Poland will have to provide any revenues to Brussels when she becomes a member state.

The own resources are "tax revenue allocated once and for all to the Union and accruing to it automatically without the need for any subsequent decision by the national authorities"[3]. They at present consist of:

1. Agricultural duties and sugar and isoglucose levies. The duties are charged on imports of agriculture products from outside the EU. As a result of GATT arrangements they largely replaced agricultural levies since 1 July 1995. The sugar levies consist of production and storage levies intended to ensure stable functioning of the sugar market. The isoglucose levies perform similar function to the sugar production levies.
2. Customs duties, which are charged according to the Common Customs Tariff on imports of industrial goods from non-member countries. Member countries to cover administrative costs of charging customs duties retain a part of these revenues (10% till the end of 2000 and 25% since 2001).
3. VAT resources: they are a part of VAT revenues collected by the member states. This part is computed according to the special procedure. In the first step, as the members vary in tax rates[4], the uniform VAT base has to be determined. To calculate it, equal sets of goods and services and standard tax rates are taken into consideration. Thus the base reflects hypothetical VAT revenues of the members and not the actual ones. The base has been capped – for example till 2006 it may not exceed 50% of the member's GNP.

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[3] *The Community budget: the facts in figures*, ibidem, p.16

[4] For example, in 1999 a reduced super rate of VAT was 1% in Belgium and 4% Italy; a reduced rate was 5% in the United Kingdom and 12,5% in Ireland; a normal rate was 15% in Luxembourg and 25% in Denmark.

The second step in computing VAT payments consists of applying a 1% rate to the VAT base and of deducting the gross compensation paid to the United Kingdom (see more below). What remains is a national contribution to the general budget. The method ensures that the actual VAT resource is less than 1% of the VAT base.

4. GNP resource is calculated according to the uniform rate applied to the members' GNP. Its aim is to balance the general budget so the rate is not known in advance. It is established during the budgetary procedure to complement the other revenues if they are not sufficient to cover the expenditure, as a ratio of lacking funds and 1 per cent of the EU GNP. Therefore the rate varies according to annual financing requirements, for example it was 0,339% in 1995 and 0,534% in 1999[5].

The first two categories are called *traditional own resources*. The revenue provided by the system of own resources is supplemented from other sources, being now of minor importance (category: "miscellaneous"), like interest on late payments, fines, surplus from earlier years and tax and social security contributions deducted from salaries of Community officials. All this money covers the expenditure in the budget for a given year.

The size of the budget and the role of various categories of resources underwent big changes since 1971 when the system was introduced (see table 1).

Table 1. The own resources, 1971 – 2000 (in EUR million)

Type of revenue	1971		1979		1988		2000[a]	
	Amount	%	Amount	%	Amount	%	Amount	%
Agricultural duties	713,8	30,6	2143,5	14,4	2605,8	6,2	2038,4	2,3
Customs duties	582,3	25,0	5189,1	34,8	9310,2	22,3	11665,3	13,0
VAT			4737,7	31,8	23927,6	57,2	34048,6	38,1
GNP					4445,8	10,6	37805,1	42,3
Miscellaneous	1033,2	44,4	2821,2	18,9	1554,0	3,7	3883,2	4,3
Total	2329,3	100,0	14891,5	100,0	41843,4	100,0	89440,6	100,0

[a] Budget 2000

Source: The Community budget: the facts in figures, 2000 edition. Offices for Official Publications of the European Communities, Luxembourg 2000, table 4.

[5] *Financing the European Union. Commission Report on the Operation of the Own Resources System,* COM (1998) 560 final, p.4.

The value of own resources grew systematically together with processes of widening, deepening and enlarging of integration in the EU as well as due to increases in price level. As it is evident from table 1 data, the growth was much bigger at the beginning of the system (within first 7 years the value of own resources increased more than six times, within last 12 years it increased barely more than 2 times). The slowing down would continue at least till 2007, when the new financial perspective enters into force. Within the own resources the category of "miscellaneous" almost disappeared and the role of customs duties and agricultural duties systematically diminished. They were substituted at first by the VAT revenues and then, in the 1990', by the GNP contributions.

The evolving structure of own resources was due to "external" and "internal" factors. The first group reflects the general tendencies in the world economy and in economic policies. Among the most important were higher inflation in the 1970' than in the 1990', liberalisation of trade in manufactures that resulted in lower customs duties, and the change in doctrine concerning the role of the state budget in promoting economic growth. Without any doubt the policy of curbing deficits in national budgets had an impact on the inclination of member states to increase financing the expenditure at the EU level. The second group of factors reflects the progress in creating the customs union, the single market and then the economic and monetary union. These successes went together with the need for more money to finance new areas of common policies. Besides, the initial enthusiasm for the community method of integration slowly vanished and the intergovernmental method gained in popularity (we shall refer to this evolution in the next section).

The gross contributions of the current members to the general budget are shown in Table 2. These figures are politically important because in the view of general public they show the costs of integration, even if in fact they are a very inadequate approximation of these costs. In absolute terms the biggest support came from Germany, France, the UK and Italy. The most characteristic tendency seems to be the closing gap between their roles in providing revenues, for example in 1995 the Italian payment was about 30%, while in 2000 it reached over 50% of the German one. This was due not to the smaller funds from Germany but to the larger flows from Italy (as well as from France and the UK). Therefore it is clear that Germany limited its leading role in financing the European integration. The other feature relates to the positions of cohesion countries. They either increased their shares in own resources, like Spain and Ireland, or kept them intact (Greece, Portugal). It may be the beginning of policy of more even distribution of budgetary costs among member states.

Table 2. Own resources by member states, 1995 – 2000

State	1995		2000[a]	
	Amount	%	Amount	%
Belgium	2680,1	4,0	3243,8	3,6
Denmark	1295,4	1,9	1682,4	1,9
Germany	21324,1	31,4	21599,0	24,1
Greece	985,2	1,5	1362,5	1,5
Spain	3645,2	5,4	6268,6	7,0
France	11876,8	17,5	14255,8	15,9
Ireland	664,8	1,0	983,3	1,1
Italy	6411,7	9,5	10804,6	12,1
Luxembourg	167,6	0,2	194,6	0,2
Netherlands	4349,6	6,4	5248,2	5,9
Austria	1762,9	2,6	2107,8	2,4
Portugal	864,9	1,3	1198,5	1,3
Finland	887,4	1,3	1218,5	1,4
Sweden	1658,3	2,4	2476,4	2,8
United Kingdom	9251,6	13,6	12913,5	14,4
Total	67,827,6	100,0	89440,6	100,0

[a] Category "miscellaneous" included in the Total

Source: The Community budget: the facts in figures, 2000 edition. Office for Official Publications of the European Communities, Luxembourg 2000 tables 18 and 33.

3. The evolution of the system of own resources

The system of own resources is a historical category and not a result of a consistent overall concept of European public finances. Politicians and bureaucrats from the member states shaped it according to the current needs of the Community and to their views of economic integration. It was started without any separated financial means. At the beginning, when the Treaty of Rome entered into force, the general budget consisted only of national contributions. Consequently, like in traditional international organisations it became totally dependent on external funding and any delays in members' payments could effectively stop or postpone the implementation of common programs.

The success of customs union and gradual widening of integration prompted the European Council to give some financial autonomy to the Community, making it less dependent on member states' transfers. Accordingly, a system of own resources for the general budget started to operate since 1971. From the very beginning it was to consist of customs duties, agriculture levies (including sugar levies) and of 1 % of VAT base. In fact only the two first resources became available due to deep differences in indirect taxation among members. But in 1979, after partial harmonisation of VAT, this third resource became feeding the budget as it was initially planned. Such a formula of the own resources meant significant financial independence of the Community from the member states allowing it to function like a true supranational institution.

However, the problems with the system of own resources began as early as in 1976, when it turned out that the available revenues were not sufficient to cover the expenses. The income from customs rates was lower than expected because of the growing role of intra-community trade in total EU trade, because of free trade agreements signed with main partners from EFTA and because of general decrease of tariffs in world trade. The income from agriculture levies was also affected as the Community was approaching self-sufficiency in food sector. The accession of Greece in 1981 created extra demand for Community funding and the increased pressure on more revenues. So, paradoxically, the successes of the EU integration contributed to the shortages in the community public finances. But beside these rather technical difficulties concerning the amount of necessary income, which were solved by adequate augmenting of VAT rate (such was 1,4% rate, introduced in 1984 in anticipation of accessions of Spain and Portugal), there emerged some more fundamental questions relating to the very nature of the system.

The general reproach was that it was unjust. As injustice is not a scientific concept and as introducing ethical values into international integration is rather difficult, its interpretation in the intra-EU relations was based on political arguments and discretionary criteria. For example, some members could not accept that that their payments unduly exceeded the receipts, i.e. they considered their net contributions as excessive. The United Kingdom was first to effectively protest against such a situation. But the correcting mechanisms, which were introduced as early as in 1975, i.e. only 2 years after its accession, failed.[6] It was not before 1984 when the British government succeeded in negotiating a permanent rebate in payments to the budget. It was calculated as two-thirds of the difference between the UK's percentage share of VAT payments to the budget, and the UK's percentage share of common expenditure that can be

[6] See: R. Bladen-Hovell and E. Symons – *The EU Budget*, in: M. Artis, N. Lee: *Economics of the European Union. Policy and Analysis*, 2nd edition, OUP 1997.

allocated to member states.[7] This refund was financed "jointly and severally" by remaining members, with exception of Germany that, as the biggest contributor, was granted a rebate in its share of the UK rebate. The compromise was a political success with vast implications. It complicated the system in technical terms. In economic terms it drew attention to the overall efficiency in using Community money. In political terms it demonstrated that the European integration could be reduced to pecuniary matters, contrasting with its early romantic vision as a tool of international solidarity aiming at prosperous, peaceful, unified and democratic continent.

The British rebate did not remedy an equity deficit of own resources. From the very beginning regressive nature of the system stemmed from the fact that tariffs were highest on food and clothing, the goods that were relatively more important for poor groups of consumers. They were more numerous in less prosperous countries. After few years when the VAT resource gained in importance, this deficiency was strengthened and became more evident. The consumption of goods and services – a basis for VAT – constituted a lower percentage of GNP in richer countries, so consequently they bore a relatively smaller financial burden than less wealthy members did. Such a situation was not only "unjust" but also unfeasible from the point of view of further integration, which could contribute to more income divergence between the "North" and the "South". Therefore the preparations for the single market programme prompted the EU to modify its public finances in order to support structural adjustments to more competition, especially in less advanced countries and regions. Their number increased a lot after accession of Spain and Portugal in 1986. As a result once again within few years the amount of own resources became not sufficient for implementing common programmes.

To remedy the shortcomings of regressivity and inadequacy, the system required deeper changes than before. In 1988 the European Council in Brussels introduced them within the so-called „Delors I package", reforming also the expenditures side of the budget and its procedures. The revenue side was upgraded with a new, fourth resource. It was a contribution based on members' GNP providing both more equity to the system and more revenues to finance new goals of structural policy. Its amount was calculated as a residual transfer, being a difference between expenditure and planned income from the three original resources. The role of GNP resource was to balance the budget. The European Council also decided to establish a ceiling to the total amount of own resources, which could be assigned for Community expenditure. It ensured more discipline in spending and introduced a long-term factor to the budgetary issues. The first ceiling for 1988 amounted to 1,15 per cent of Community's

[7] Ibidem, p.380.

GNP and was gradually increased to 1,2 per cent in 1992 within the so-called Financial Perspective for the period 1988 – 1992. Introduction of the GNP resource was combined with the limitation of the importance of the VAT resource. Its base was capped at 55 per cent of members' GNP to make own resources less regressive. In economic terms this connection related the VAT resource to the GNP level increasing the actual role of the latter in determining the contributions of members to the common budget (GNP roughly equals value added in the national economy).

This direction of reforms in the system of own resources was continued after the Treaty on European Union was signed, within "Delors II package" approved by the European Council in Edinburgh in 1992. Between 1993 and 1999 (the second Financial Perspective) the ceiling for own resources was further increased from 1,2 to 1,27 per cent. In order to eliminate differences in the calculation of GNP in member states, the European System of Accounts was developed in 1995 and introduced in 1999. From 1994, the VAT base for cohesion countries (Greece, Ireland, Portugal and Spain) was limited to 50 per cent of GNP and for remaining members gradually reduced in order to reach this threshold in 1999. The role of this resource was further diminished by gradual lowering of maximum VAT call rate from 1,4 per cent in 1995 to 1 per cent in 1999. Consequently, as the revenues from customs and agriculture duties almost stagnated, the share of GNP resource increased from 11 per cent in 1988 to over 48 per cent of the total budget in 1999. "Delors II package" provided stability in a system for many years.

In 1999, the European Council in Berlin approving the third Financial Perspective for 2000 – 2006 kept the 1,27% ceiling intact, which – in the perspective of budgetary needs of the next enlargement – might be somehow surprising, not only in the candidate states[8]. This policy of tight budget was also different from approaches reflected by two previous perspectives from 1988 and 1992, when the resources were increased. The Council neither introduced any changes into the system itself, although it accepted the critical evaluation of the own resources done by the European Commission[9]. According to the Commission's report, the system was not entirely satisfactory. It provided adequate financing, ensured equity in contributions and was cost-effective (i.e. the procedure of funds collecting was not expensive). However, the Commission pointed out as its disadvantages the lack of financial autonomy, as

[8] Jean-Pierre Chevalier – *L' accord interinstitutionel du 6 mai 1999 et les perspectives financieres 2000-2006: des nouvelles ambitions pour l'Union europeenne?*, Revue du Marche commun et de l'Union europeenne, no. 441, septembre 2000.

[9] *Financing the European Union. Commission Report on the Operation of the Own Resources System*, COM (1998) 560 final.

well as not transparent and complicated procedures of collecting the EU money. The growing role of the GNP resource began in fact a retreat from policy which was at the birth of the system and which gave the EU finances the attribute of supranationality. This in turn was considered a part of the successful method of integration distinguishing the EU from other groupings. For the lack of simplicity in the system several solutions were responsible: capping of VAT base (and making VAT resource a GNP resource); difficulties with identifying which member state actually provided traditional own resources (for example, the customs revenues collected in Rotterdam not necessarily resulted from duties imposed on imports to Holland); as well as complicated mechanisms of calculating the UK rebate.

Having shared the Commission's concerns, but ignoring its proposals to find a new category of own resources, better suited to the needs of deepening integration, the European Council in Berlin decided to postpone deeper reforms till the end of the present Financial Perspective, correcting in the meantime the inequity aspect of the system as more sensitive and urgent for political reasons.[10] The following new measures were taken:

1) Since 1 January 2001 the percentage of traditional own resources retained by the members to cover the collection costs was increased from 10 to 25%;
2) The maximum rate for the VAT resource would be decreased to 0,75% in 2002 and 2003 and to 0,50% in 2004 and later;
3) The share of Germany but also of Austria, the Netherlands and Sweden in financing the UK rebate was lowered to 25 percent of their normal share. The rebate will not include the windfall gains resulting from changes in the financing systems and from future enlargements;
4) All GNP estimates for the own resources must be based on ESA 95 national accounts system making GNP equal to gross national income (GNI).

It would be difficult to qualify these amendments as coherent with the evaluation of the Commission, which we mentioned earlier. First of all by strengthening the role of GNP resource, they consequently weakened autonomy of EU public finances. Like it was before 1970, the common programs would be subordinated to stricter control of member states whereas one could expect that deepening and widening of European integration would require transferring power to the Commission and the Parliament. In the Commission's report the financial autonomy was explicitly considered as important factor for deepening integration. Second, leaving more money to the members to compensate for collection costs might contradict the Commission's opinion that the system of

[10] Council Decision of 29 September 2000 on the system of the European Communities' own resources (2000/597/EC, Euratom), OJEC, L 253/42.

own resources was cost-effective. It rather suggests that it was the other way round and that the Council expects these additional funds to become an incentive to the member states to look more vigorously for customs and agriculture duties, thus contributing to more revenues in the common budget. Third, introducing new rebates from the UK abatement will hardly make the system more transparent and comprehensible for the EU citizens, as the Commission postulated.

The direction of these modifications seems, however, coherent with the evolution of the system of own resources after the 1970'. On one hand, the independence of the EU public finances has been consequently limited. On the other hand, "fairness" has dominated other important aspects of its construction, like economic efficiency, becoming a hot issue in political debates over distribution of benefits from integration. The level of "fairness" was identified with a net contribution to the budget (i.e. the balance between the payments and receipts) *per capita* relative to member states' wealth. For the public opinion these indicators were straightforward measures of economic benefits gained by the member states. Table 3 illustrates the basic example of the latter approach.

Table 3. Net contributions to the budget of the European Union in 1997 (millions of ecus and %) and GNP per head in member states

State	Amount	% GNP	GNP per head in PPS
Belgium	1079,5	0,50	115,3
Denmark	68,6	0,05	112,5
Germany	-10943,5	-0,60	109,4
Greece	4371,8	4,13	69,0
Spain	5936,0	1,28	77,7
France	-781,1	-0,06	104,3
Ireland	2676,7	4,84	82,4
Italy	-61,3	-0,01	102,6
Luxembourg	725,4	4,89	176,2
Netherlands	-2276,2	-0,71	106,0
Austria	-723,6	-0,40	112,6
Portugal	2721,8	3,12	69,6
Finland	56,1	0,06	96,4
Sweden	-1129,5	-0,59	93,7
United Kingdom	-1798,8	-0,16	100,3
Total	-78	-0,00	100,0

Source: Financing the European Union. Commission Report on the Operation of the Own Resources System, COM (1998) 560 final, Table 5 and Annex 8 Table 4.

According to the criterion adopted in Table 3, the biggest beneficiaries were Luxembourg, Greece, Portugal, Spain Ireland and Belgium and the costs of integration were borne mainly by the Netherlands, Germany, Sweden and Austria. This structure hardly reflected the ranking of the relative prosperity of the members. It would be difficult to explain the voters, why the countries with lower incomes have to support richer members. It would be especially difficult in case of such closely connected neighbours as Belgium and the Netherlands, Germany and France as well as Sweden and Finland. The corrections introduced by the Berlin European Council for the payments of Austria, Germany, the Netherlands and Sweden temporarily remedied this situation but they are by no means a final solution of the equity problem in public finances.

Table 4. Share in 3rd and 4th resources and in GDP by member states in 2000 (%)

State	3rd and 4th resources (1)	GDP[a] (2)	Balance (1)-(2)
Belgium	3,0	3,0	0,0
Denmark	1,9	1,7	0,2
Germany	25,7	23,2	2,5
Greece	1,6	1,9	-0,3
Spain	7,6	8,6	-1,0
France	17,8	16,0	1,8
Ireland	1,1	1,1	0,0
Italy	13,3	15,2	-1,9
Luxembourg	0,2	0,2	0,0
Netherlands	5,1	4,8	0,3
Austria	2,6	2,4	0,2
Portugal	1,4	2,0	-0,6
Finland	1,5	1,4	0,1
Sweden	2,9	2,4	0,5
United Kingdom	14,2	16,2	-2,0
Total	100,0	100,0	0,0

[a] current market prices, PPS

Source: calculated on basis of Annex Table 6, European Economy 2000 no. 70 and table 32 in: The Community budget: the facts in figures, 2000 edition. Office for Official Publications of the European Communities, Luxembourg 2000.

The net-position may be a good criterion to evaluate budgetary costs and benefits from integration but it is not a proper basis to calculate who pays too much or too little to the own resources. Looking from this point of view one should exclude traditional own resources, which cannot be allocated to the particular member state, and should consider only relative VAT and GNP contributions.

Both are presented in Table 4 and compared with GDP (as a proxy for GNP) to show the level of equity in the present system. Ideally, if the system were "fair", the share in payments from the 3rd and 4th resources should be the same as the share in the total GDP. If the state pays "too much" relative to its wealth, its share in the two resources is bigger than in the GDP – and vice versa.

In 2000, according to this criterion, the least encumbered were the United Kingdom and Italy, not the least prosperous members. Their benefits were equal to the benefits of the four cohesion countries taken together. On the other hand, the most burdened were Germany, France and Sweden. The conclusion is that there are good arguments to develop a general mechanism equalising financial contributions to the Community budget, basing them on clear principles.

4. Implications of the approaching enlargement

The process of enlargement to the East seems one of the most important challenges faced by the European Union at the beginning of the 21st century. There is little doubt that the accessions of the former communist countries will influence the absolute size of the common budget, change its structure and contribute to the reevaluation of the whole system. In particular the revenue side of the budget will have to be thoroughly analyzed and probably reformed. The latest moment is the year 2005 because the new financial arrangements must start in 2007. If, according to the Nice and Goeteborg Summits, the real date of enlargement is year 2004, it means that the decisions may be made without new members (before 2004), or in 2004-2005 with those who will have finished the negotiations and will have qualified to the club. It is rather obvious that the second option would build more confidence between the EU and the candidates.

Regardless of the option chosen by the EU-15, sooner or later the new enlargement will increase contributions to the budget. First, the new member states will provide additional revenues. For example, the estimates for Poland's payments vary between 2,272 and 2,354 billion euro, depending on several assumptions concerning the level of GNP and exchange rate[11]. The actual strength of this impact will be moderated by several factors. One of them is the strategy of enlargement. If the convoy scenario materialises, i.e. the candidates not accede one by one but as a group, or more probably – in some sub-groups, it would more radically increase the size of the EU finances. These new payments however may not appear in the budget right after the accession. In this area of negotiations all candidates from the former communist countries asked for transition periods. For example Poland expects 5-year prolongation before paying full contribution and plans to start with 90% reduction in 2003 (the expected date of accession) increasing the payments by 20 percentage points each consecutive year.

It is reasonable to assume that the EU side will accept easing the burden for the candidates, although the schemes may be different from their proposals. First, there was such precedence during former enlargements. Second, transition period for budgetary payments is a technical measure of political importance, in a sense, because it does not undermine the single market or disrupt the market mechanisms, or distort common policies. It requires some generosity, however. Obviously Poland (like other candidates) will have problems with finding enough money for paying her share. In theory, her contribution would be compensated by funds available in the framework of common policies. But in reality these money might not appear as Poland lacks necessary experience and administrative apparatus for using them. No transition period in such a situation would make her a net contributor to the budget instead of a net beneficiary. This could slow down the economic growth after accession as well as have a disastrous effect for the social perception of the process of integration. Both are not in the interest of the EU either and it is well known that the complicated conditions of obtaining the EU money are too difficult even for present members who often do not spend all the funds they are eligible for. Such a failure in the case of a newcomer is much more probable.

Beside growing number of member countries, there is another reason, which makes probable bigger size of the common budget. The fact that the present candidates are less developed than the members is one of the reasons why the want to join and why the EU has been reluctant to accept them. Their accession in most of the cases will require long-term substantial financial support from the common budget. The income gap is too big to be significantly diminished in a few years time, even if candidates grow much faster than the EU. In order to limit amounts spent on new members the Berlin European Council decided that the EU funds couldn't exceed 4% of a national GNP.

[11] See: E. Kawecka-Wyrzykowska, S. Ładyka – Szacunek wpłat Polski do budżetu UE i transferów z unijnego budżetu do Polski (mimeo), IKiCHZ, Warszawa, grudzień 1999.

According to the European Commission estimates supplying the extra money will worsen the present members' budgetary positions by ca 0,15% of their GNP[12]. Provided the *status quo* is maintained on the income side and there is no restructuring in the expenditures, it means the own resources' ceiling growing roughly from 1,27% to 1,42% of GNP. This, however, seems unlikely because of the strategy of tight budget initiated during the Berlin Summit. Such an increase would also require approval by the national parliaments, which would be hard to achieve. Therefore more probable is the abandoning of present policy of keeping expenditures at 1,09 % of GNP. The margin between 1,09% and 1,27% could accommodate additional budgetary burden of the enlargement[13].

But the main problem is that the average burden will not be evenly distributed. If the present mechanism is maintained the United Kingdom will pay a smaller fraction due to its rebate. Relatively less affected will also be Austria, Germany, the Netherlands and Sweden, the countries that are the biggest net contributors and that recently obtained rebates in financing the British abatement. It means that the enlargement is likely to renew discussions among the present members about their contributions to the common budget rather than to start such a discussion between them and the new ones.

Poland, as well as other candidates, has been very cautious in formulating opinions about the own resources mechanism. When accession negotiations began, the official view was presented in Poland's position paper on "Budget and Finances"[14]. Poland fully accepts *acquis communautaire* in this area and declares its implementation since the day of accession. This commitment applies also – in general – to methods, rules and procedures of the system of own resources.

The need for a bigger budget will further increase the share of the GNP resource or will prompt searching for new sources of Community money. The first scenario seems more likely because it simply has more supporters than the second one.[15] They have some strong arguments. First, there is no satisfactory candidate for the new own resource. The idea to collect revenues

[12] Financing the European Union, ibidem, p.27.

[13] As Mr. Jacek Saryusz-Wolski, *Secretary of state in the Committee for European Integration concluded "it is not possible to have bigger Europe for less money"*, Ani tak, ani nie, Gazeta Wyborcza, 27.02.2001.

[14] See: Poland's position papers for the accession negotiations with the European Union, Government Plenipotentiary for Poland's Accession Negotiations to the European Union, Chancellery of the Prime Minister of the Republic of Poland, Warsaw 2000.

[15] It seems that only Belgium and the European Commission are strongly in favour of an EU tax. See: *Prodi calls for tax to fund EU budget*, Financial Times, May 30, 2001.

from possible new taxes (CO_2 emissions tax, various corporate taxes, personal income tax and various indirect taxes) although technically feasible has not met with approval of the EU institutions. Technically, neither of them ideally fulfils the Commission's criteria of financial adequacy, equity, cost-effectiveness, autonomy and transparency. But what is more important, they better fit politically into federal concepts of integration. Therefore they could be seriously considered "over the long term", if the EU adopts such a model that would require more autonomy of its finances.[16]. The profits earned by the European Central Bank from seigniorage would seem another obvious "own resource". The only problem is that not all EU members belong to the EMU and not all of them contribute to the creation of ECB profits. This leads us to the second point – even if the new "European" resource is selected, the governments of member states will have to determine the rate at which it will be levied.

Domination of GNP resource will be strengthened also because enlargement will increase the number of relatively poor countries and their bargaining power. This group will be particularly sensitive to any inequity in the system of own resources. Therefore they will favor the GNP based contributions as the fairest resource from the point of view of members' ability to pay. Whether the formula relating these contributions to the GNP will be regressive, neutral or progressive is another question of political nature. But regardless how the governments define „fairness", with dominating share of GNP-based income in the whole revenues the name "own resources" will become somewhat inadequate.

With the perspective of enlargement the British rebate will inevitably return to the EU agenda. But the candidates will rather not open the discussion during the negotiations because the problem is more serious than just the amounts redistributed through this instrument. In fact it concerns the very idea of public finances in the EU. For example Poland in negotiation position simply accepted paying a share "reflecting her economic status". Many experts in the EU question maintaining the rebate[17]. Its disadvantages are numerous. First, due to the rebate the own resources lose the systemic nature and become a discretionary set of rules. Any exception for one member encourages others to present their demands for reductions. It undermines the system and makes it less transparent. Deficiencies of such a solution will be more pronounced with more governments involved in bargaining over proper amounts of national contributions to public finances. Second, the budgetary situation of the UK vis-à-vis living standards in the EU is different than in the past when the rebate was

[16] Financing the European Union, Annex 2.

[17] See for example Ch. Franck et al. – *Europe's political priorities report*, Draft Report, September 2000, TEPSA (mimeo) p.16.

introduced. Now the others could start asking for "their money back". In addition the accession of poor countries will decrease the average income in the EU that serves as a benchmark for member's ability to pay. In effect, the relative prosperity of all present members will improve and some of them may not qualify for the support received before enlargement. In other words the number of net contributors should increase if the rules of the game are to be respected. But it will be difficult to persuade the cohesion countries about necessary sacrifices if more affluent members managed to negotiate reductions in their shares of the revenues. In sum – positive reaction of richer states to the needs of the poorer partners will confirm that ideas of European unity and solidarity are still valid.

The system of own resources is only a small element of a very complicated machinery of European integration. It is less spectacular than the rest of these elements but not less important because it constitutes a fundament of public finances in the EU. It is very much contingent on all other policies, far beyond economic sphere. Analyzing its history one can learn how the politics of integration have evolved. The member states do not devote much effort to the reforming of own resources mechanism although it does not operate satisfactorily. Its role and shape in the future will depend on the general concepts of integration and these do not seem clear. For example, it is difficult to forecast how popular will the option of "strengthened cooperation" be among groups of members wanting to deepen integration in selected areas. If the member states choose this way, then public finances based on GNP contributions will be a logical consequence. If the federal vision prevails, they will have to reconsider returning to the idea of autonomous sources of common finances and to supplement traditional own resources with a new one of similar nature[18].

[18] Jean Monnet advocated an independent budget for the Communities. See: J. Pinder, *European Community. The building of a Union*, OUP 1991.