Key Issues for Consultation

Introduction

In Briefing Paper 2 we set out how the EU budget is constructed. This showed some areas where there are problems with the current approach to budgeting both on the income and on the expenditure side. This briefing paper sets out some of these difficulties under thematic headings.

Context for Change

The EU budget has been very resistant to change. The last major reform took place in 1988. Since then some significant changes in EU structure and policy have taken place:

- The EU has increased from 12 Member States to 27
- The EU internal market developed significantly
- The Euro has been introduced in a many Member States
- The EU has extended its ambitions as a global actor with regard to both development assistance and international security policies
- The Lisbon Agenda for Growth and Jobs has been agreed
- The EU response to terrorism has had significant policy implications both in its internal policies under the heading of 'Justice and Home Affairs' and in terms of its external policies as set out in the European Security Strategy[1].

Given this set of changes, it may be surprising that the budget has not kept up with the changes around it. Iain Begg, in his paper 'The 2008/2009 Review of the EU Budget: Real or Cosmetic?'[2] compares some aspects of the EU budget for the period 1988–1992 (period A) with the period 2007–2013 (period B), showing how little has really changed:

- The budget ceiling has gone from 1.2% of GDP to 1.24% of GNI[3] representing only a marginal change
- The actual expenditure commitments were budgeted in period A at 1.17% and turned out at 0.99% of GDP; for period B the planned expenditure commitments are at 1.05% of GNI

There are other facets where more change is evident. The share of the Common Agricultural Policy (CAP) has gone from 51.4% of the budget in period A to 32% of the budget in period B. The share of the budget allocated to cohesion spending has moved from 30.2% to 35.6% in the same period.

Administrative expenditure is a small proportion of the budget for both periods but slightly higher for period B (6%; as compared with 4.7% for period A).

[1] Accessible at: http://www.consilium.europa.eu/cms3_fo/showPage.ASP?id=266&lang=en&mode=g

[2] Accessed at: http://www.cesifo-group.de/pls/guestci/download/CESifo%20Forum%202007/CESifo%20Forum%201/2007/forum1-07-special1.pdf on 7 January 2008

[3] GDP (gross domestic product) and GNI (gross national income) are different measures of a countries financial status; GNI = GDP plus the net flows of income such as rents, profits, and labour from abroad. For the EU as a whole the difference between the two is marginal but there are some marked differences for individual countries. Germany, the UK, France, the Netherlands, Italy, Belgium, Sweden, Denmark, Finland and Austria all have significantly higher GNI than GDP so contributions to the EU budget based on GNI will be higher than if based on GDP. The other Member States have a GDP which is either only slightly lower or higher, and in some cases significantly higher, than the GNI. The countries with the most largest difference between GDP and GNI in this direction are Ireland, Poland and Spain.

Where there has been more of a change, generally outlined in Briefing Paper 2, is in the source of EU income between the two periods 1988–1992 and 2007–2013[4]:

Source of Income	1988 to 1992	2007 to 2013
VAT	58	16
GDP/GNI	9	69
Traditional Own Resources	33	15

This shows that even though technically the income of the EU is still an own resource, most of the funding now comes from sources which are economically inter-governmental transfers. The shift between VAT and GDP/GNI resources also poses the question what purpose the split serves. One of the obvious simplifications that could take place as a result of the review would be to remove this split completely.

Finally, there is the question of so called corrective mechanisms or abatements. The only formal abatement in both periods is the UK rebate. However, even when this was negotiated, Germany had an implicit rebate in a limitation of its contribution to the funding of the UK rebate which, by the current period (2007 to 2013), was extended to the Netherlands, Austria and Sweden, through the Inter-institutional Agreement which governs the Medium-term Financial Framework or Financial Perspectives.

Some other special arrangements have been negotiated which also distort, if only slightly, the framework which on the face of it appears relatively simple.

How big should the budget be?

This is the question that tends to dominate the discussions in the run-up to each new Financial Perspective (now renamed Medium-Term Financial Framework) – but is it the right question? Should not the budget be decided on the basis of the policies of the EU and a discussion as to whether and when it is better to spend at EU level rather than at national level or even more decentralised levels? We return to these questions later.

Compulsory and Non-compulsory Expenditure

Some treaty obligations into which the EU has entered give rise to expenditure which is deemed compulsory. The most important one of these is expenditure on the Common Agricultural Policy which was written into the Treaty of Rome[5]. Whilst the Treaty does not specify the level of expenditure or the share of the budget, the policy itself is a treaty obligation. Where expenditure is deemed compulsory, the European Parliament has significantly less power than on other expenditure. This, it could be argued, removes the Common Agricultural Policy, at least to some extent, from democratic scrutiny at EU level.

The Common Agricultural Policy (CAP)

Apart from the issues referred to above, there is the question of the CAP more generally. The CAP continues to absorb a significant proportion of the EU budget and lack of reform to reduce expenditure in this area will limit the room for manoeuvre for reform and changes in priorities in other areas.

A review of the CAP will run in parallel with the review of the budget. While noting that they are two different reviews rather than two aspects of the same review, there is scope for arguing some principles for change within the CAP in the context of the budget review, too. For more information on this, see Briefing Paper 5 in this series.

Flexibility

In budget terms, flexibility is generally not an easy concept. A budget, once set, is a base line against which actual income and expenditure can be measured and so should not be changed. So we do not mean flexibility in

[4] Iain Begg, The 2008/2009 Review of the EU Budget: Real or Cosmetic? For website details see Footnote 2 above.

[5] Founding Treaty of what is now the European Union

terms of altering the balance of the budget in respect of the total available, in terms of where there money comes from, or how it is spent.

Rather, flexibility can be seen in allowing a certain amount of movement between headings of planned expenditure in the light of actual expenditure: when a particular programme has worked well then it should be possible to allocate funds in excess of budget from areas where programmes have not worked well.

Flexibility also means that over time it should be possible to alter priorities to reflect changes. The 7 year Financial Perspectives restrict flexibility because the framework, once set, is difficult to change before the end of the period. A system of rolling medium term plans might make the whole system more flexible.

Another issue of flexibility is the question of budget years and the extent to which expenditure can be moved from one year to the next. If it is difficult to get a programme started, especially at the beginning of a new Financial Perspectives period, funding for it may be lost.

A good example of timing issues is the newly created Stability Instrument. This instrument for external action in situations of crises in third countries was introduced in the 2007 to 2013 Financial Perspective but was only finalised very late in the preparatory phase. The first annual action programme was not signed off until the end of 2007 so that all expenditure that could have happened in 2007 will now take place in 2008; but even then, the calls for proposals for implementing the Annual Action Programme are not likely to be published until the first quarter of 2008 leaving only 9 months for decision making and implementation. There will come a point when any money not spent will be 'lost' – i.e. contribute to an underspend which will generate a surplus. The EU, however, does not create any reserves for future use out of such underspends; rather it reduces the Member State contributions for the following year by an equivalent amount.

Flexibility in the current system is strictly limited to the following:

- Some limited movement between and within headings of the financial framework
- European Aid Reserve[6] (up to € 0.2 bn per year)
- European Globalisation Adjustment Fund[7] (up to € 0.5 bn per year)
- Solidarity Fund[8] (up to € 1 bn per year)
- Flexibility Instrument[9] (up to € 200 bn per year)

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[6] To be able to respond rapidly to specific aid requirements resulting from events which could not have been foreseen when the budget was established, the Commission's Humanitarian Aid Department may also call on an Emergency Aid Reserve (title 40). For this to be mobilised, the Commission, the Council and the Parliament must all agree. (http://ec.europa.eu/echo/finances/budget_en.htm on 3 January 2008)

[7] The EGF aims to help workers made redundant as a result of changing global trade patterns to find another job as quickly as possible. The fund was launched by the European Union in 2007. Information accessed on 3 January 2008 at: http://ec.europa.eu/employment_social/egf/index_en.html

[8] To enable itself to respond in a rapid, efficient and flexible manner to urgent situations, the Community has established a Solidarity Fund. This will intervene mainly in cases of major natural disasters with serious repercussions on living conditions, the natural environment or the economy in one or more regions of a Member State or a country applying for accession. Information accessed on 3 January 2008 at: http://europa.eu/scadplus/leg/en/lvb/g24217.htm

[9] Established in the interinstitutional agreement of 6 May 1999, the flexibility instrument permits the budgetisation of €200 million cumulatively over three years for matters that could not otherwise be financed in each budget year. Information accessed on 3 January 2008 at: http://ec.europa.eu/budget/other_main/glossary_en.htm#F

Accountability and the Planning Cycle

The planning cycle of the EU budget is, as has been mentioned before, based on medium-term financial frameworks (MFF). These were added to the annual budget negotiations in 1988 and since then have been the following:

'Delors Package 1':	1988 to 1992	5 years
'Delors Package 2':	1993 to 1999	7 years
'Agenda 2000':	2000 to 2006	7 years
Current MFF:	2007 to 2013	7 years

The MFFs have helped to reduce the difficulty of agreeing a budget each year which had become an increasing feature of the 1980s; having these planning frameworks has thus ensured some stability. However, there are some flaws in the system.

The term of the European Parliament and the European Commission does not cover the same period as the MFFs.

For example, the initial plans for the current MFF were set out by the Prodi Commission which concluded its term in November 2004. The Barroso Commission then took over the negotiation of the packages up until it was agreed and will be responsible for the implementation of the first 3 years of the MFF. A new Commission will take over in 2009 and the extent to which it will be made up of current and new Commissioners will not be known for some time. In other words, the Commission responsible for the bulk of delivering the current MFF (2010 to 2013) will have had no part in designing it.

Similarly, the European Parliament which was instrumental in agreeing the current MFF will be subject in June 2009 to elections that will determine who has the parliamentary responsibility for turning the MFF into annual budgets and programmes.

The other part of the budget authority, the Council, is made up of the representatives of the Governments of the Member States. They, too, change. The changes at Member State level happen on different cycles in different countries and could not be brought in line with a budget or financial planning cycle at EU level.

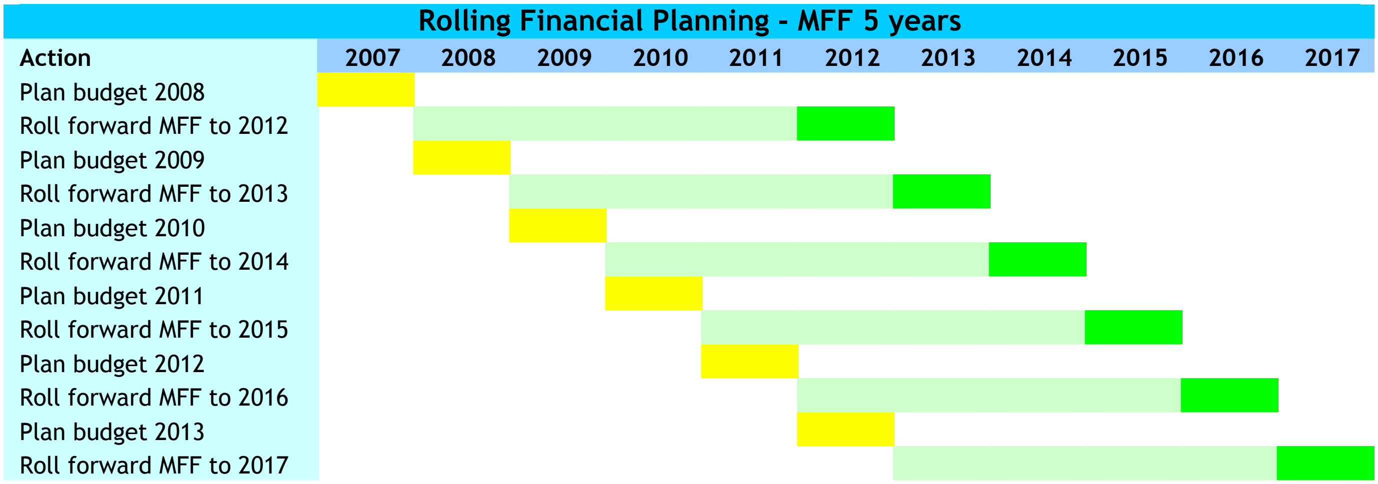
The question arises of how to solve this problem of accountability. There are, essentially, three options, assuming that going back to basic annual budgets is neither possible nor desirable:

1. The planning cycle could be brought in line with the terms of office of the European Parliament and the European Commission which are broadly similar. The European Parliament is elected in the summer and begins work in September; the Commission is nominated during the summer and confirmed by the Parliament in the autumn. All this happens in the same year and on a 5 year cycle. If the MFF were on the same cycle the Commission and Parliament responsible for its implementation would be different from the Commission and Parliament that drew it up.
2. The planning cycle could be brought in line with the terms of office of the European Parliament and the Commission but be rolling at mid-cycle. That would mean each Commission and Parliament would be involved in drawing up a MFF and implementing the first half of it.

In both these cases, reducing the planning cycle from 7 to 5 years would lead to some incentives on the part of each Commission and European Parliament to take full ownership of the planning mechanisms.

3. A more radical approach, and one which I have not found referred to in any of the literature on this subject, would be to have MFF on a rolling basis That would mean that each year the budget for the next year and a further year of the MFF would be under discussion. The benefit of this would be to allow an

annual look at fine-tuning the MFF but at some remove (i.e. the fine-tuning would affect year 6 in a 5 year planning cycle). An example of how this would work is shown below in diagrammatic form:



This approach would have the benefit of:

- Making annual and regular both the annual budget process and the MFF planning process, in which those responsible could become expert and where expertise could be handed on relatively smoothly
- By allowing an annual look at where the MFF is going, changes in policies and priorities can be reflected within a foreseeable timeframe without unpicking the agreement for the medium term.

The drawback of this approach would be one of annual budget discussions – even if the main issues under consideration are some time in the future. It might be possible to move to such a system gradually.

Balance between policy priorities

The problem of timing and timeframes also affects the issue of policy priorities. These change over time and if the budget planning cycles lag behind the policy development by several years then that affects the effectiveness of policy decisions at European level.

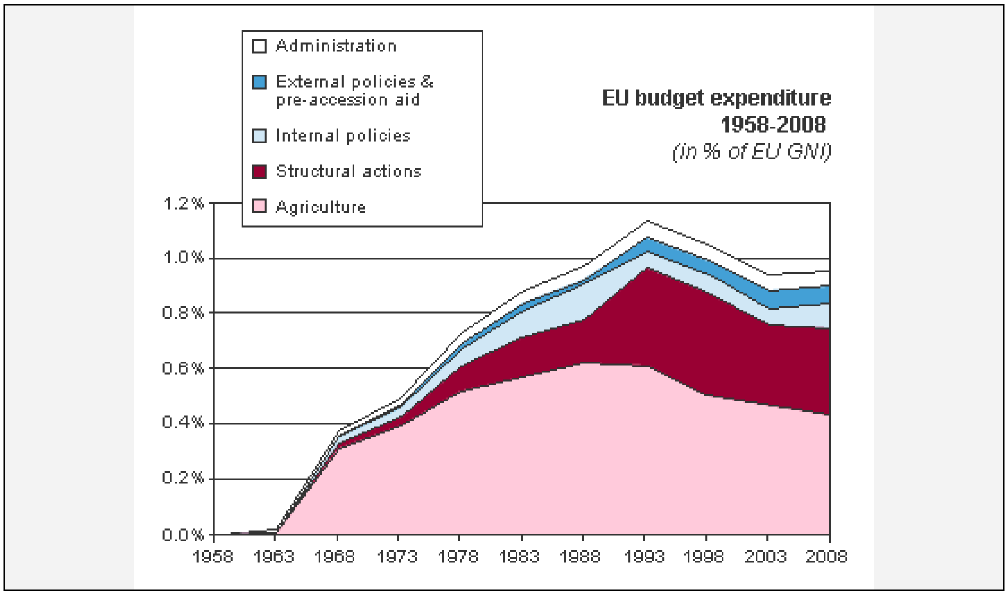
This can be demonstrated with the following example:

The sequence of decisions: (the 2000 to 2006) medium-term financial framework (‘Agenda 2000’) was elaborated by the Santer Commission, even before the actual launching of the Euro and the conclusion of the enlargement negotiations with Central and Eastern European candidate countries, then negotiated by national representatives over the winter 1998-1999, to be finally adopted, with great difficulties, in the Berlin summit of April 1999, precisely at a time when, in the aftermath of the Russian financial crisis, some European economies, and especially Germany, were experiencing a marked slowdown in economic activity, which luckily appears, in retrospect, to have been very short and probably overestimated. Exactly one year later, in a context of euphoria about the ‘new economy’ and booming economic activity all over Europe, while the first signs of a recession were being felt in the US, the Lisbon Council meeting, elated by the good economic performance of the EU and the success of the new currency, then widely believed to function as a shield protecting Europe from the negative effects of the US recession, adopted the ambitions objectives of the Lisbon strategy. But the structure of the EU budget had been frozen for seven years the year before…[10]

[10] Jacques Le Cacheux, Funding the EU Budget with a Genuine Own Resource: the Case for a European Tax, Notre Europe, May 2007, accessed at: http://www.notre-europe.eu/uploads/tx_publication/Etud57-FundingtheEUBudget_02.pdf on 8 January 2008

This very clearly demonstrates how the budget planning cycle constrains the EU's ability to move forward within a reasonable timeframe on policies it has agreed.

A budget should be a reflection of what an organisation or institution wants to do; i.e. it should reflect its priorities. An area of activity with a large budget allocation should also be one of the policy priorities. In the European Union, the relative weight of different policy areas in terms of budget allocation has shifted significantly over recent years.



Spending on the Common Agricultural Policy as a percentage of the budget has decreased, despite the fact that a number of the more recently joined Member States have significant agricultural sectors. See Briefing Paper 5 in this series for more detail on the Common Agricultural Policy.

Resources for cohesion and competitiveness (providing both for assistance to those regions or Member States which are less well off and assistance to Member States more generally to improve their competitiveness in a global market) has increased in terms of its importance in the overall budget and is set to overtake agricultural spending during this Financial Perspective.

Both of these policy areas have a redistributive effect within the EU – i.e. they move resources from one place to another. In the case of the CAP, this is to those countries with significant agricultural sectors and within those countries to farmers. In the case of the cohesion and competitiveness budget it is to Member States which are poorer and/or less competitive but without targeting one particular sector of the economy.

Between them, these two elements of the budget make up almost 80% of the budget leaving less than 25% for all other policy areas and administration. Administration makes up very little of the EU budget, a fact that is sometimes overlooked when the media and some politicians delight in being critical of the overblown Brussels bureaucracy. In fact, the EU has a rather small staff and a large proportion of the staff is engaged in tasks directly related to the EU operating with 23 official languages.

The EU policy area entitled 'Citizenship, Freedom, Security and Justice' is a relatively new one which, though only absorbing a small proportion of the budget, is likely to increase in importance in the foreseeable future.

The EU as a global actor, i.e. the funding the EU has available for its external action, also has only a small share of the budget, currently around 6% of the total. This has been a relatively constant proportion over many years. At the same time the European Union has increasing ambitions to be seen as a global actor playing its role on a global stage; the financial means for this are not keeping pace with expectations.

In addition to the funds available within the budget envelope, The EU has access to the European Development Fund. This money is available for Official Development Assistance provided primarily to the so called African, Caribbean and Pacific countries. This is governed by the Cotonou Agreement[11] and is extra-budgetary.

Balance between EU level and MS spending/subsidiarity

The EU budget comes from the Member States and, as we have seen in Briefing Paper 2, most is also spent in Member States, so much of the EU budget is about shifting money around between them. Is that useful? And is it necessary? Clearly, for a number of reasons it is. But what should the balance be?

'In the budget as elsewhere, European action should provide clear additional benefits compared to action by individual Member States alone in pursuing policies that promote the European common interest.'[12]

So how do we define 'clear additional benefits'? The issues are of subsidiarity and proportionality.

Subsidiarity

The principle of subsidiarity is defined in Article 5 of the Treaty establishing the European Community. It is intended to ensure that **decisions are taken as closely as possible to the citizen** and that constant checks are made as to whether action at Community level is justified in the light of the possibilities available at national, regional or local level. Specifically, it is the principle whereby the Union does not take action (except in the areas which fall within its exclusive competence) unless it is more effective than action taken at national, regional or local level. It is closely bound up with the principles of proportionality and necessity, which require that any action by the Union should not go beyond what is necessary to achieve the objectives of the Treaty.[13]

Proportionality principle

Like the principle of subsidiarity, the principle of proportionality regulates the exercise of powers by the European Union, seeking to set within specified bounds the action taken by the institutions of the Union. Under this rule, the institutions' involvement must be limited to what is necessary to achieve the objectives of the Treaties. In other words, the extent of the action must be in keeping with the aim pursued.

This means that when various forms of intervention are available to the Union, it must, where the effect is the same, opt for the approach which leaves the greatest freedom to the Member States and individuals.[14]

These principles also apply to the budget. Clearly, there are some policy areas where only European level intervention will work. These are policy areas with transnational dimensions, with significant potential for economies of scale, where a critical mass is required that would exceed the capacities of a Member State or where there are issues of coordination at stake.

There should therefore be some criteria which clearly define when it is appropriate to spend at the European level rather than at Member State level. Some criteria could include the following:

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[11] Partnership Agreement Between the Members of the African, Caribbean and Pacific Group of States on the one Part and the European Community and its Member States on the other Part, 2000, accessed on 7 January 2008 at: http://ec.europa.eu/development/icenter/repository/agr01_en.pdf

[12] Reforming the Budget, Changing Europe – A public consultation paper in view of the 2008/2009 Budget Review, European Commission, 12.9.2007, accessed on 3 January 2008 at: http://ec.europa.eu/budget/reform/library/issue_paper/consultation_paper_en.pdf

[13] From: http://europa.eu/scadplus/glossary/subsidiarity_en.htm accessed on 3 January 2008

[14] From: http://www.euramis.net/scadplus/glossary/proportionality_en.htm accessed on 3 January 2008

- Efficiency: i.e. pooling resources, avoidance of duplication, and economies of scale
- Spillover effects: ensuring that when spending in one territory impacts on another territory these spillover effects are positive rather than negative; a good example would be transport networks where people from different territories or jurisdiction benefit from a network, the cost of which falls disproportionately on one or more of the territories or jurisdictions concerned.
- Fiscal capacity: where the intention is to achieve cohesion across the EU, this can only be achieved at EU level because the poorer Member States would not have the fiscal capacity to support their poorer regions whilst the richer countries do. This could also be expressed as the budgetary dimension of solidarity.

EU – Added Value - How is that Defined?

The question of which policy areas are necessary, at what level of detail and where the benefits of the European Union in these terms lie is a very complicated one. Looking at the European Commission website, and in particular on the page entitled 'EU Policies', there is a long list of well over 100 policy areas which are diverse and encompass many fields which would also seem at home in domestic policy frameworks. There is therefore a huge degree of overlap between Member States and the EU in these terms. This is unavoidable, not least because many of the EU policies are internal in nature.

In this context it is then very difficult to define what represents added value. One of the ways in which it could be defined is to say that expenditure being incurred at EU level should reduce the public expenditure burden by avoiding duplication and unhelpful competition between the Member States and by economies of scale. At the very least, the public expenditure burden should not be increased by spending at EU rather than national level.

Unfortunately all too often the debate is not about the added value of EU spending in these terms or the benefits of the EU policies but rather about the net contribution, which Member States generally seek to minimise, i.e. ensure that the budget remains small, that policies benefit them financially or, that if they do not, that some special measures are included to reduce their net contribution.

What could be achieved in the budget review?

First and foremost, the budget review offers an opportunity to turn the debate away from the 'minimise the contribution, maximise the receipts' approach of Member States to one which starts from policy objectives. This might mean removing the rigid ceiling of the EU budget of 1.24% of GNI. This represents such a small proportion of the total public expenditure incurred in Europe that even significant changes in absolute terms would only have marginal effect on the tax burden on citizens. The European Union of 27 has a population of 495 128 529. The current level of budget equates to a tax burden of around € 255 per annum per head of population. So there should be some scope for change without causing significant problems. Of course, a larger budget could only be justified if the policies funded had widespread support and were supporting the core values and priorities of the European Union.

Secondly, there should be a way of demonstrating the added value of EU spending which is simple and transparent enough to make sense to citizens.

Thirdly, significant changes to the Common Agricultural Policy would allow some room for manoeuvre in the remainder of the budget. See Briefing Paper 5 in this series for further details on this.

Fourthly, there could be significant change in the way the EU budget is funded (see below).

Finally, the timing of budget decisions could be reviewed to make it more flexible and more transparent.

A new funding structure

There are, essentially, only three means by which the EU can be funded:

- Through a system of real own resources, i.e. income which the EU has of right and not as a result of transfers from Member States, calculated on whatever basis
- Through transfers or contributions from Member States
- Through a combination of these two systems.

The current system is the third of these with the transfer from Member States having increased over time as a percentage of the total. As it is a combination of the two pure methods, the advantages and disadvantages of the two pure methods apply to this method, too, but in proportion to the weight each method has in the combination.

Advantages and Disadvantages of a Pure Own-Resources System

A pure own resources system would allow the EU to budget on the basis of a balance between the available finance and the policy priorities – similar to the governments of the Member States. If the source of the funds is not related directly to a factor which identifies the amount of it coming from each of the Member States, then it would lead to less discussion about net contributions.

The disadvantages of such a system relate to the predictability of the level of income (or rather the lack of predictability) and the need to identify a means of generating such income. The customs revenues and levies on agricultural exports are not generating enough, as can be seen by the current system, so the only viable alternative to this would be some form of EU level tax; i.e. a tax which the EU could levy itself and could decide on itself.

We will outline below in a bit more detail the options for an EU tax and some of the reasons why it might be difficult to arrive at this solution.

Advantages and Disadvantages of Transfers from Member States

This system provides certainty about the level of resources available to the EU. Once agreed, Member States are committed to the amount of money they have to contribute. It does, however, leave the control of the size of the EU budget firmly with the Council, with the European Parliament having a much smaller say, because a budget has to be agreed and the Council decides on this on the basis of unanimity. It is, of course, conceivable that even with this type of funding mechanism the decision of the Council could be on the basis of qualified majority voting. However, and because the system is much more about the ‘perceived cost’ to the Member States, it is less likely that this would be possible.

The disadvantage of this method is an inbuilt tendency to the lowest common denominator effect. Again, this is partly affected by the Council having to decide unanimously but partly also by the focus on ‘perceived costs’ rather than on policy objectives.

A Tax at European Level

Introducing a new tax is never easy. Introducing a tax at European level, especially at a time when enthusiasm for the European project, at least in some Member States, is not at its highest, would be difficult.

There are some criteria which should apply to all taxes levied by any government or governmental structure. Any tax developed at a European level would have to be tested against those criteria.

- It should be simple and transparent
- It should be buoyant – in other words, as wealth increases, tax revenues should benefit
- It should have a broad base – in other words the number of tax payers should be as great as possible
- It should be at a low marginal rate – in other words each tax payer should pay as little as possible whilst achieving the desired tax revenue
- It should deliver ‘horizontal equity’ – in other words ‘equal treatment of equals’
- It should deliver ‘vertical equity’ – in other words those who can pay more should pay more.

At a European level, there are a number of other criteria which might need to be considered.

- The first is the question of tax competition. Are there taxes which, levied at national level, lead to competition between Member States (horizontal tax competition) and is that a positive or negative trend? Can a European level tax be seen to be of benefit overall here?
- There could also be competition between Member States (or even public authorities within Member States) and the European level (vertical competition). Again, this could have positive or negative effects.
- As in the criteria of horizontal and vertical equity mentioned above, this also needs to apply at the level of the component parts (i.e. fairness among the Member States)

With this in mind, below is a critical assessment of a range of EU level taxes which have been put forward by a number of writers on the subject:

Type of Tax	Issues Raised
VAT	Technically quite simple; some VAT already assigned to EU; but: different levels of VAT in different Member States[15]; the money generated by each Member State from VAT is more than would be required for the EU budget so the EU would need only a 'slice' of the VAT income; by making it an EU tax, the European Parliament would have the power to vote on the EU VAT rate; the tax would still be collected by Member States, along with their own share of the VAT revenue, and the EU 'slice' would be transferred. However, VAT is seen as a regressive tax (i.e. less well off citizens tend to spend more of their money (rather than saving it) and thus pay VAT on a larger proportion of their disposable income. To an extent, this is off-set by reduced rates of VAT (or that is the theory) but with the variety of rates and products and services they apply to in different Member States, there would certainly be some questions relating both to horizontal and vertical equity.
Excise Duties	These are taxes or duties levied on certain goods such as alcohol, tobacco and fuel. They currently apply in many countries[16]. ♦ Alcohol: the EU has some regulations in place but there is significant variation in the rates of duty that apply and some alcoholic drinks (e.g. wine and sparkling wine) do not have any duty levied on them in some countries; making this a tax at EU level would require a common approach. ♦ Tobacco: All EU Member States levy a specific tax on cigarettes but not on all tobacco products; making this a tax at EU level would require a common approach. Fuel: Whilst some or all fuel is taxed in all EU Member States, there are variations in the rates and in the types of fuels to which this applies: making this a tax at EU level would require a common approach.

[15] There are different rates of VAT applicable in different Member States. The Standard Rate ranges from 15 to 25%; all Member States also have reduced rates (some only one, some up to 3), and these range from 2.1 to 17%; the types of products and services which reduced rates apply to also vary from one Member State to another, as do the products and services which are either zero rated or exempt from VAT.

[16] Information about these taxes in EU Member States accessed on the European Commission website on 10 January 2008 at: http://ec.europa.eu/taxation_customs/taxation/excise_duties/energy_products/rates/index_en.htm

Type of Tax	Issues Raised
Eco-tax	This would be taxes levied on activities which are damaging to the environment and could have, *inter alia*, the following effects: ♦ Increasing the cost of such activities, thereby discouraging them ♦ Countering the effect of 'the race to the bottom' if such taxes were imposed by EU Member States at different levels ♦ Levying a tax on activities which, though often undertaken in one Member State, have potentially detrimental effects over a wider geographic basis. However, if the tax were effective at discouraging the activity, then it would not be buoyant and thus potentially not yield enough revenue to fund the desired budget.
Communication Tax	This would be a tax on activities such as using mobile phones or SMS; the rationale here is that this is a large market, that decreases in the cost of technology are a direct result of a large market and that the tax would therefore be both at a low marginal level and at the same time buoyant in terms of revenues generated. The question of why this would be levied at EU level is hard to answer as there must be more intra-country traffic than international traffic of this type.
Corporate Tax	There are currently different corporate tax systems in different EU Member States; this contributes to the movement of employment between Member States as companies, especially those companies for which it is not important where they are located, seek out locations with low corporate tax burdens. This would be ameliorated to a certain extent but as corporate tax is not the only factor influencing the location decisions of companies, this would not solve all the problems. However, as a growing number of corporations are multi-national, there is a very good case to be made for EU level taxation.
Personal Income Tax	This would operate no differently to the income tax paid at national level. There might be a degree of resistance to it but it would provide a very direct link between citizens and the EU. On the principle of 'no taxation without representation' this would introduce the taxation which should go hand in hand with the representation at EU level in a very direct way. Issues both of horizontal and vertical equity would, however, arise as the standard of living and thus incomes vary significantly between and within Member States. However, as long as the EU 'slice' of personal income tax is below the lowest level of income tax levied in any EU Member State this is may be of limited concern. A benefit of using an income tax is that, unlike VAT, it is progressive rather than regressive in nature.
Savings Tax	This would be a tax on income from personal financial assets. Such assets are currently taxed in all EU countries[17] and moving to taxation at EU level could lead to the removal of horizontal competition. Some harmonisation for non-residents holding savings in a Member States has already taken place through the 'savings directive'[18] so this could be seen as a further development.

There are likely to be significant political obstacles to having a European level tax, not least because the introduction of any new tax is not likely to be popular even if this would be cost-neutral to tax payers. Nor is it likely to be popular with national governments to hand over control of revenue generation to decision making at European level. That said, the budget review should not start from the question of what might be politically

[17] Jacques Le Cacheux, Funding the EU Budget with a Genuine Own Resource: the Case for a European Tax, Notre Europe, May 2007, accessed at: http://www.notre-europe.eu/uploads/tx_publication/Etud57-FundingtheEUBudget_02.pdf on 8 January 2008

[18] Accessed at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2003:157:0038:0048:en:PDF on 10 January 2008

do-able at this point but from the question of what is desirable in terms of funding the EU. That is, to enable the EU to be funded in a transparent and clear way that generates sufficient funding for the EU budget to achieve the political objectives of the EU and that ensures a direct relationship between the citizen and EU which encourages accountability and engagement. A tax levied at EU level might possibly bring this about.

Part of what the consultation might usefully have addressed is the question of whether EU citizens might be willing to have an EU level tax and, if so, what type of tax they would favour. Although the consultation does not specifically ask that question, it is still worth commenting on this in any response to the consultation, not because it will have immediate impact but because it might contribute to a shift in thinking.