SEMINAR : EU BUDGET : WHAT FOR ?
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The EU budget as an instrument to finance collective goods: Key points for the debate
Yves Bertoncini

The core idea I would like to express is that, to be meaningful, the discussion on the EU budget, its value added and its revision must absolutely be undertaken on the basis of a wide economic, financial and political vision. The "Centre d'analyse stratégique" is currently working in this perspective and my objective here is only to tell you about the three main directions we are following.

1 – A wide economic vision: the EU budget is only a "subsidiary" tool.

1.1- The European and national budgets can't face all the challenges EU and its member states are confronted with. For each of these challenges, they must be considerer as a possible tool, as well as :

- the political tool : to promote Europe at the international level, the definition of common diplomatic positions can be much more important that the fact to spend more money;
- the regulatory tool : to promote growth and competitiveness, the extension and good functioning of the single Market seem to be essential;
- the private financing tool : when some funding is needed, the intervention of the European Bank of Investment, the promotion of public private partnerships or the rise of households' spending can be as useful and efficient as public spending – a symbolic example : 2/3 of the 3% of GDP EU objective for R&D concern private spending.

1.2. The use of non budgetary tools seems to be particularly important as regards the principal sectors financed by the EU budget :

- as far as CAP is concerned, the level of public spending is narrowly connected to the evolution of the regulatory framework (customs duties and direct support to farmers);
- as far as EU cohesion is concerned, the regular "Reports" produced by the Commission show that the impact of market dynamics (including foreign direct investments) is at least as important as the one of public spending;
- as far as the Lisbon strategy is concerned, academic studies regularly show that public regulatory interventions and private financial investment are crucial for the improvement of R&D, education or infrastructures.

2 – A wide financial vision: the need to focus on all European public spendings

2.1. It's almost absurd to deal with EU budget without taking into account national and regional budgets:

- EU budget often co-finances actions and projects in cooperation with Member states, regions etc.;
- the "three pillars" structure of the EU illustrates the diversity of European cooperation, which can rely principally on Member states, including financially;
- the development of Open Methods of Coordination confirms the need to consider what the Member states are doing and spending : it's particularly true for the Lisbon strategy, whose main guidelines must be implemented by EU countries and budgets.

2.2. Only a global vision of European public spending can show what are the priorities for the EU and its countries:

- this global vision helps to establish the real hierarchy of public spending in Europe : for example, the average CAP spending corresponds to 0,5% of EU GDP (but ¾ is financed by the EU) R&D public spending to 0,8% of EU GDP and Education spending to 5,2% of EU GDP.
- on the basis of this hierarchy, it's easier to evaluate the situation of EU public spending when compared with its principal competitors (USA, Japan, emerging countries etc.) and to identify in which sectors more or less public spending would be desirable;
- the global vision of European public spending also makes it easier to assess the repartition between national and EU levels and to identify in which sectors EU should do more or less.

2.3. As such a global vision of EU public spending doesn't exist today, the "Centre d'analyse stratégique" decided to collect all the data available, sectors by sectors, so as to produce a comprehensive Report in July 2007. We hope than the European institutions will regularly undertake such work in the future.

3 – A wide political vision: the role of the EU budget can't be defined only on the basis of technical justifications

To define what the EU budget should finance or not, it's not enough to establish the presence of "externalities" or "economies of scale" and necessary to take into account:

3.1. The diplomatic compromises which determined the structure and level of the EU budget, on the basis of many elements (budget efficiency, compensation of costs-benefits of the commercial integration etc.);

3.2. The so called "collective preferences" of the Europeans, whose visions and needs can differ largely on some points;

3.3. The other examples of "fiscal federalism" (USA etc.), provided the comparison is made keeping in mind the difference of the socio-political contexts.

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22 JANUARY 2007

TECHNICAL NOTE FROM THE GENERAL SECRETARIAT

THE EUROPEAN REGIONS IN THE SINGLE GLOBAL MARKET: THE CHALLENGES FACING REGIONAL POLICY FOR THE PERIOD 2014-2020

CONTENTS

Introduction

Rarely will a European debate have been shrouded in such uncertainty as the one that is opening up today on the future of EU policies and the place of regional policy and the regions in this new configuration. There are two main reasons for this uncertainty:

- first, concerning the form of the debate: hardly a year after agreement was reached in December 2005 on the financial framework for the programming period 2007-2013, the "*rendezvous* clause" sets the date for a review of the EU budget in 2008-2009. This calls for urgent and rapid reflections but reduces the time we have available to really take account of what has been achieved in 2000-2006, let alone 2007-2013. This makes any serious forecasting of the challenges of the next period very difficult, and forces us to fall back on a forward studies approach, with its share of uncertainties. It was an excellent idea to allow time for a debate, and it was doubtless necessary to hasten the process, but we cannot exclude the risk that this will result in a loss of substance.
- Secondly, the substance of the debate: the extent of the economic, technological and geopolitical changes taking place in the context of globalisation has never been so marked. A plateau seemed to have been reached in the 1990s, but the years 2000-2005 have shown that we were in fact only at the beginning of a period of even greater upheaval. China's dramatic entry on to the stage of international competition is certainly the most significant element, but it is not the only one. The revolution in information and communication technologies and the changes affecting employment are also equally crucial issues. Furthermore, most Member States had not even had time to put in place the strategy adopted in Lisbon in March 2000, when the European Union had to hastily adopt a renewed strategy in the spring of 2005 in order to give it a new impetus.

These two factors combined only serve to make the debate more complex. It is no easy task, in such a rapidly changing global context, to evaluate in 2007 what Europe's needs will be in 2014-2020. However, we can project some trends – particularly economic and demographic – with relative certainty. In view of the rapidity with which certain parts of the world are closing the economic gap with Europe, given the ease with which certain industrial sectors have completely revolutionised their production methods in a very short space of time, and in the light of the observed disparities between Europe and its main partners and competitors in terms of demographic growth or innovation potential, it has become quite clear today that Europe and the Europeans are going to have to demonstrate over the next ten years an astonishing capacity to adapt to these changes.

But this is not the most difficult task. The main challenge will be whether Europeans really will be ready and willing to go down a certain number of paths together, or whether on the contrary they will tend, slowly but surely, to fall back on national, or even on purely individual, strategies, replicating the development pattern of the large international groups which have become increasingly stateless and totally independent of any political authority (numerous highly symbolic examples have been evident in most European countries over these last few months). And what if waging a struggle against the temptations of increasingly nationalistic and individualistic behaviour were to be the only choice for the future of Europe? In such a panorama, will pro-European sentiment still be suffieciently strong at the beginning of the period 2014-2020 to allow the creation of a new European cohesion? If we listen to the opinion polls, take note of the positions of some intellectuals – even if they are in a minority –, or analyse the slow erosion of the Member States' financial commitment to Europe (in 2009 this will be lower in relative terms than in was 20 years previously before the fall of the Berlin wall), we would be tempted to doubt it.

One thing is certain however: if the great majority of political forces wish Europe to remain united to tackle these new challenges, then the citizens of Europe will have to be more involved, their voices will have to be heard and they will have to be given greater responsibility in deciding how Europe should adapt to these major changes and above all what methods should be used to successfully tackle the challenges.

The European Union will only be able to continue to exist in the global concert of nations as a group of countries that share a certain number of common values if it succeeds in uniting all its forces – civil society and political forces – and this is where the mission of the regional authorities will be of crucial importance.

In the context of globalisation, Europe will have to be citizen-inclusive and anchored in its territories, or it will not survive.

I. THIS WORLD IN WHICH WE LIVE: A BRIEF INTRODUCTION TO THE REFLECTIONS

I.1. GROWTH, COMPETITIVENESS AND COHESION

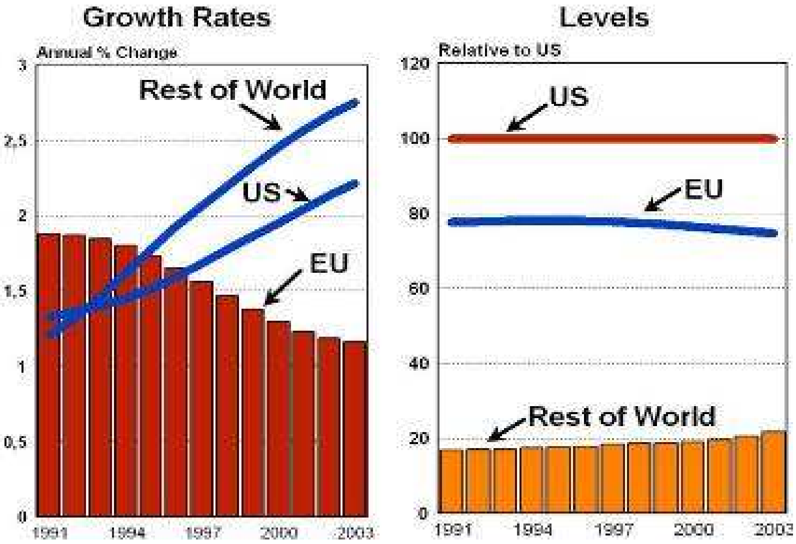
A. EUROPE IN THE WORLD

Over the last ten years, European growth has been relatively stagnant, for a number of quite simple reasons on which all analyses, whether by the European Commission, the World Bank or the OECD, for example now seem to be agreed. We have grouped these together in the following section under the headings of a number of economic and demographic observations.

A1: The development gap between Europe and the rest of the world is gradually narrowing

Europe has reached a certain level of development which makes any significant further growth much more difficult than in the past. This can be seen clearly from the analysis of disparities in productivity (GDP/economically active population). Although Europe is situated well above the vast majority of other countries, new world regions are enhancing their levels of competitiveness. The following figures illustrate this phenomenon.

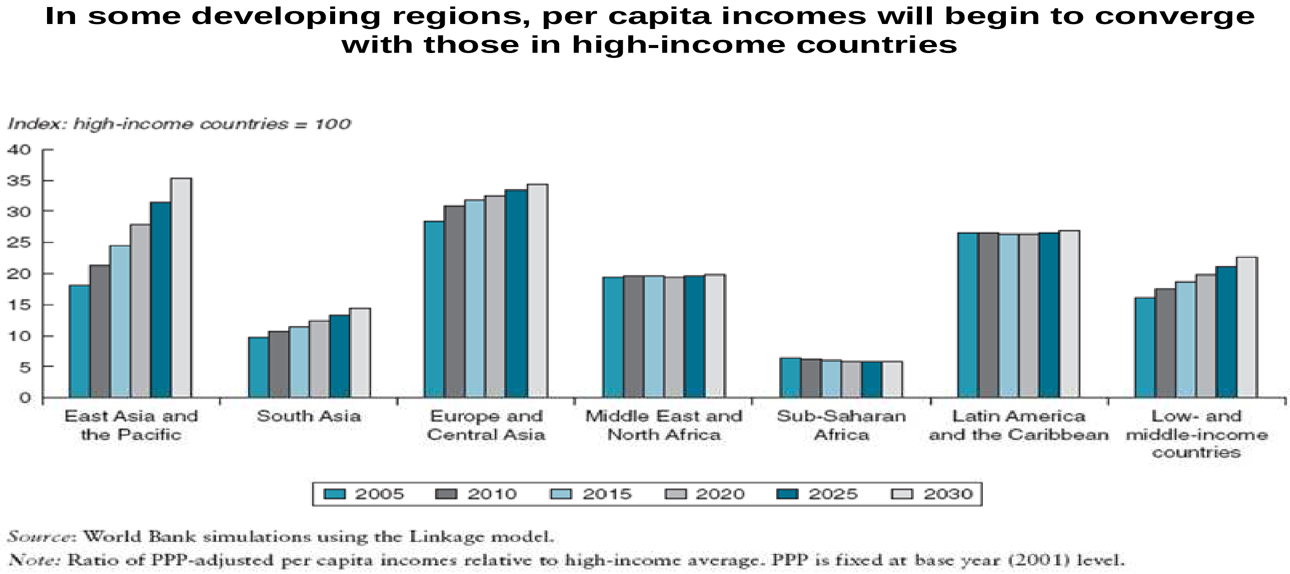
Figure 1: World labour productivity trend Europe/United States/rest of world and current disparities



Source: European Commission, DG Ecofin, July 2006.

The first significant point to note is that in terms of stock, the development gaps are still very wide but at the same time the trends are surprisingly regular. The second noteworthy aspect is the gradual widening of the gap between Europe and the United States. This overall convergence is however much more easily demonstrated if we look at major global regional groupings. Figure 2 is a forecast, made on the basis of past changes, of the extent to which the main developing regions will, or will not, catch up with the high-income countries (Europe, United States, Canada, Japan, Australia, etc.) in the next 25 years. Index: high-income countries = 100.

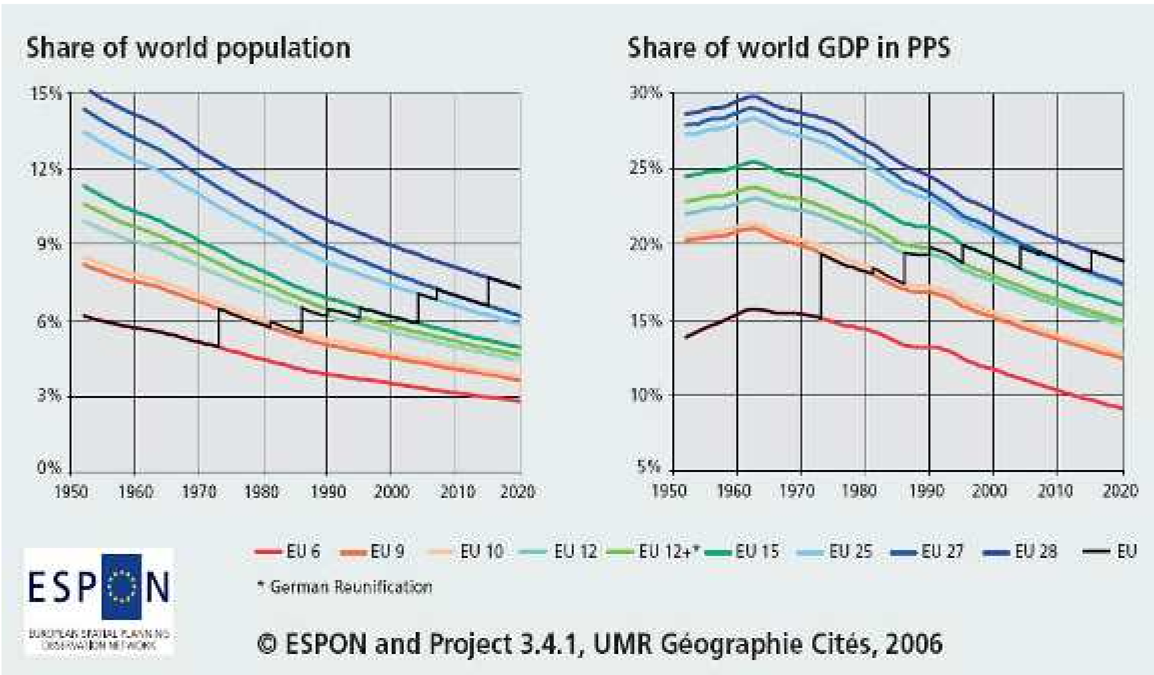
Figure 2: Forecast of the extent to which regional groupings of developing countries will catch up on the high-income countries



This convergence will essentially take place in South-East Asia, South Asia, the neighbouring countries of Eastern Europe including Central Asia, and certain middle-income countries. On the other hand, Latin America's position remains stable, as does that of North Africa and the Middle East, while Sub-Saharan Africa continues to see its position weaken.

***A2:* This convergence in growth, mostly of Asian origin, also tends to make Europe's position in the world relatively stable**

Figure3: Changes in Europe's share of world population and world GDP in the light of successive EU enlargements (1950-2020)



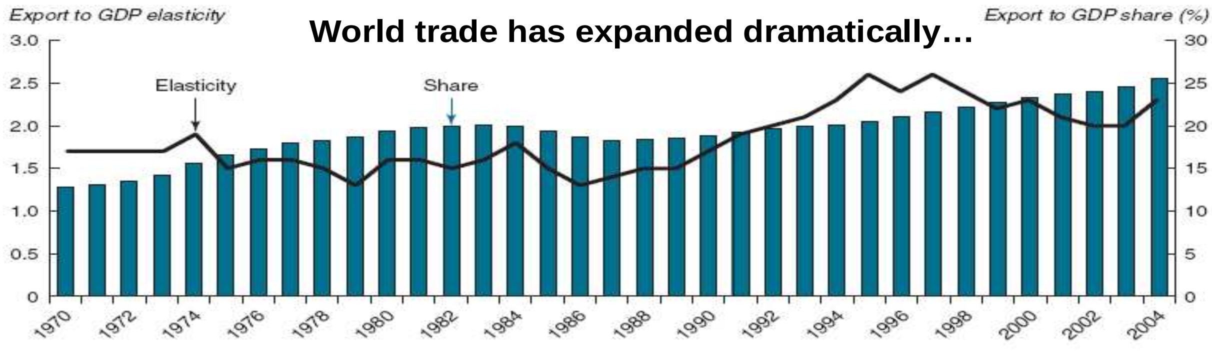
With the expansion of the EU from 6 to 15 Member States, Europe's share of world population remained at 6% between 1957 and 2004. This increased with the most recent enlargements, and will remain at 7.5% for many years to come, despite falling rates of demographic growth. However in GDP terms the picture is very different. The share of EU28 (which includes Croatia) in world GDP in 2020 is forecast as being almost the same as that of EU9 at the beginning of the 1970s, i.e. around 19%.

So, even though the effects of the single market are still fully at work, they are tending to subside in relative terms if we project current trends, and this in spite of the various enlargements.

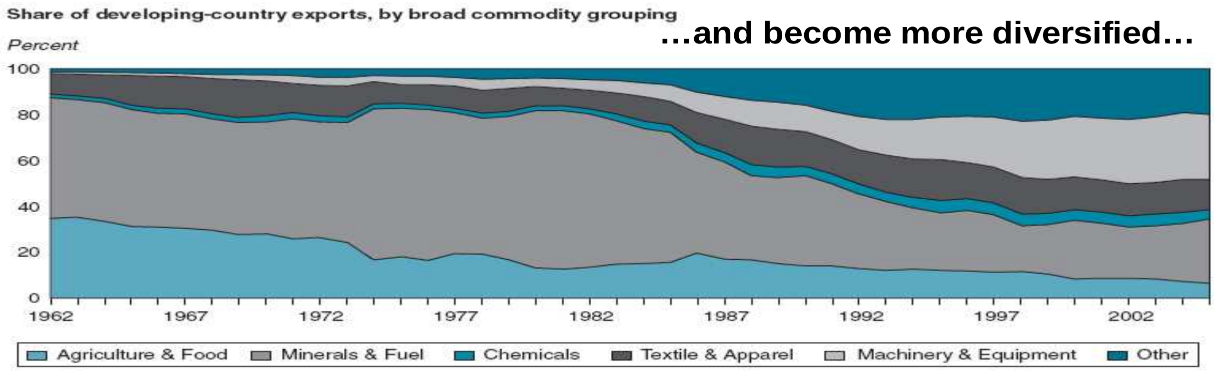
A3: Acceleration in the globalisation of trade also relativizes the positive effects of the single market

To speak of a sharp acceleration in the process of globalisation is no cliché. The latest study published by the World Bank shows that the share of trade in wealth has grown very significantly, with a clear acceleration over the past fifteen years. The measure of elasticity (the black line on the graph below) shows the difference between growth in trade and GDP growth. This has been higher than 1.5 for nearly 40 years and has more often than not been higher than 2 since the beginning of the 1990s. In 2005 trade represented 25% of world GDP, compared to approximately 15% in 1970.

Figures 4 and 5: Growth in world trade as a percentage of GDP and diversification of trade



Sources: World Bank Development Data Platform (DDP) and staff calculations.
Note: Elasticity is calculated as the percent change in real exports relative to the percent change in real GDP. The export share is calculated in nominal dollar terms. Data are smoothed using five-year moving averages.

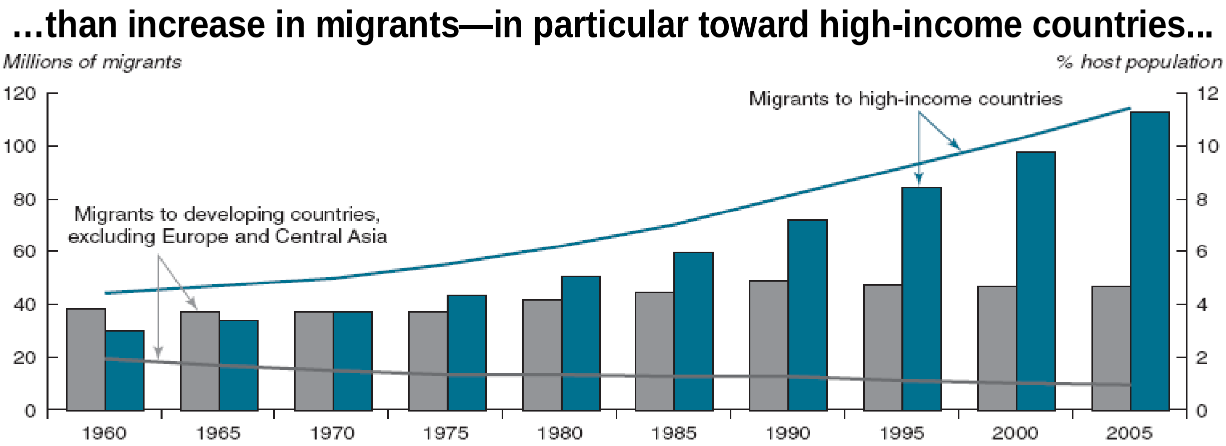


Source: World Bank World Integrated Trade Solution (WITS).

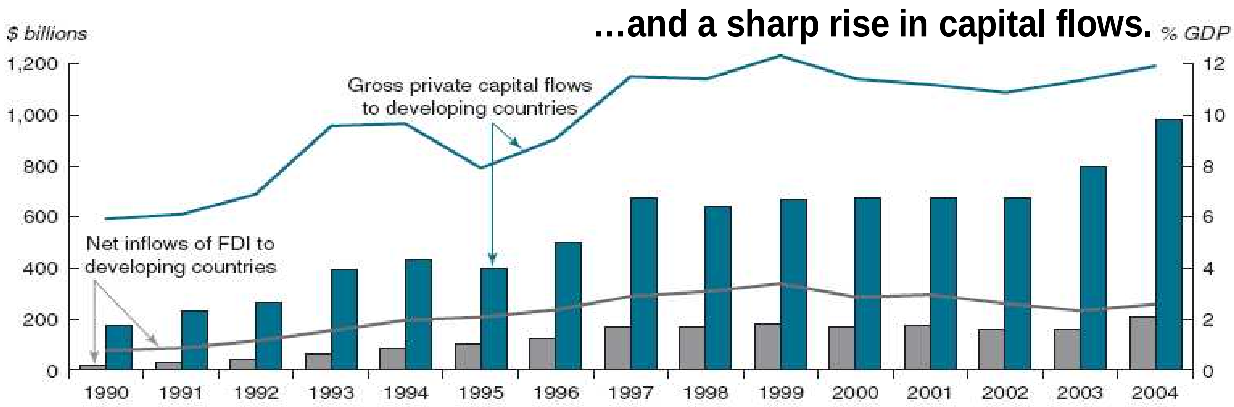
The second graph shows how the structure of world trade has changed over nearly 40 years. Until the mid-1980s, agriculture and energy represented the largest share of world trade. This has now become more diversified with manufactured goods having a larger share. This has had a much more widespread impact on European activities and on the modification of production systems.

Growth in trade is of course not the only component of globalisation. The blue line in figure 6 shows the increase in numbers of migrants towards high-income countries, reflecting inequalities in world growth. From about 40 million per year in the 1960s, the number of migrants has nearly tripled today, with a particularly sharp increase over the last fifteen years. And these figures of course only reflect official, or known, migrations. Over the same period, the numbers of migrants towards developing countries have steadily fallen. It is important to underline that while there is a close correlation between levels of development and migration, this is not the case today between growth levels and migration. The fastest-growing countries today are not necessarily those with the highest levels of in-migration, India and China being the best examples.

Figures 6 and 7: Growth in migration and in capital flows



Sources: World Bank 2006a; World Bank 2006c; staff calculations.
Note: Bars are measured on the left axis; lines are measured on the right axis.



Sources: World Bank DDP and staff calculations.
Note: Bars are measured on the left axis; lines are measured on the right axis. FDI = foreign direct investment.

The last point we want to make concerning the phenomenon of accelerating globalisation relates to capital flows. This is one of the aggregates that has seen the sharpest acceleration over the last fifteen years. Foreign direct investment in developing countries has been multiplied by five over this period. It is important to note that this investment does not necessarily relate to relocations in the sense that Europe sometimes understands them, but most of the time is investment in productive locations in response to domestic demand from new, rapidly-growing markets. Investment naturally tends to be drawn to places where demand is increasing, but it is true that at the same time it creates new skills which can then prove to be a source of competition.

These brief analyses are not sufficient to anticipate all the changes that lie ahead. Having outlined the context, the most important questions remaining are the terms of trade and the analysis of the sectors in which Europe remains, will remain or should remain competitive on a global scale.

A4: Profound changes in the terms of trade raise questions as to the future positioning of many European economic sectors

This aspect of the forward study is of course the most complex. We will address it very modestly using just a few illustrations. Figure 8 shows that the era when down-market products were traded against up-market products is coming to an end. Global competition in the future will essentially be in trade of middle- and up-market productions. China appears to have taken over world leadership for some time now in down-market products, with more than 20% of the market, and if the trend continues will shortly reach a level equivalent to that of Europe and the US put together. On middle-market products, Europe has continued to increase its production, while Japan and the United States have over the same period seen their share in the world market fall sharply. The localisation of production of this product type in the enlargement countries is no doubt a contributing factor, and the European model remains extremely competitive both in terms of market share and in growth rate. The question remains, how long will it be able to hold on to this position, and what strategic alliances will it have to make in order to do so? Europe's leadership in the up-market sector is even more clear-cut, both in terms of market share and growth, whether compared to China, the United States, or Japan.

Figure 8: Variation in world trade by type of product (down-, middle-, and up-market)

Parts du marché mondial des produits bas de gamme, moyenne gamme et haut de gamme en 2003 et évolution sur la période 1995-2003

(Niveau en pourcentage et variation en points de pourcentage)

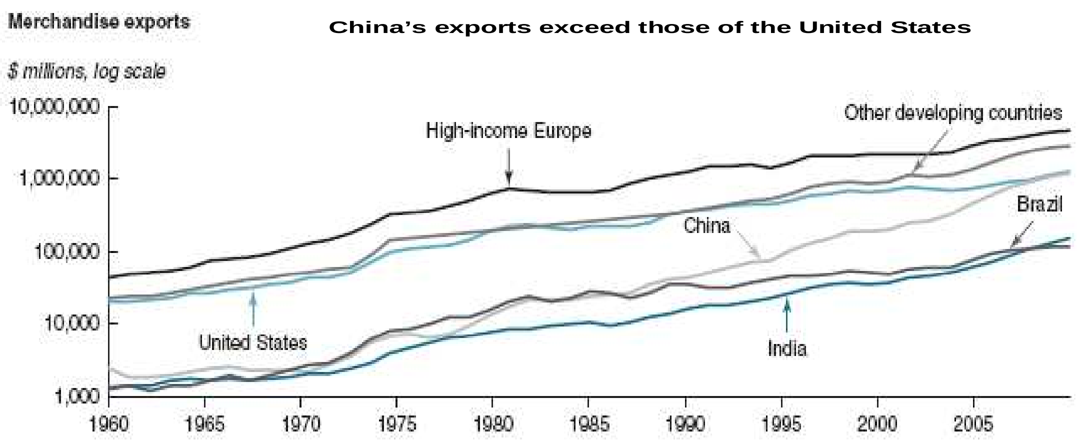
	Bas de gamme		Moyenne gamme		Haut de gamme	
	2003	Variation	2003	Variation	2003	Variation
UE	12,9	*-1,8*	20,0	*2,0*	32,3	*3,1*
Japon	6,7	*-2,2*	11,7	*-4,4*	15,2	*-6,9*
Corée	5,1	*-0,1*	4,4	*0,8*	3,1	*-0,6*
États-Unis	12,0	*-3,7*	13,6	*-4,1*	17,9	*0,2*
Chine	20,4	*8,1*	8,2	*4,6*	3,7	*1,5*
Mercosur	3,0	*0,1*	4,2	*0,6*	0,9	*-0,1*
ANASE	7,4	*-2,8*	7,7	*-1,5*	5,3	*-0,3*

Source: UN Comtrade – Calculs du CEPII (2006) – Rapport pour la DG Commerce

It is worth highlighting the position of China, which has increasingly strengthened in recent years. Figure 9 below shows that China has just overtaken the United States in the export of manufactured goods, while the high-income countries of Europe continue to hold world leadership. The European model remains extremely competitive. Everything will now depend on the capacity of a certain number of sectors to remain competitive.

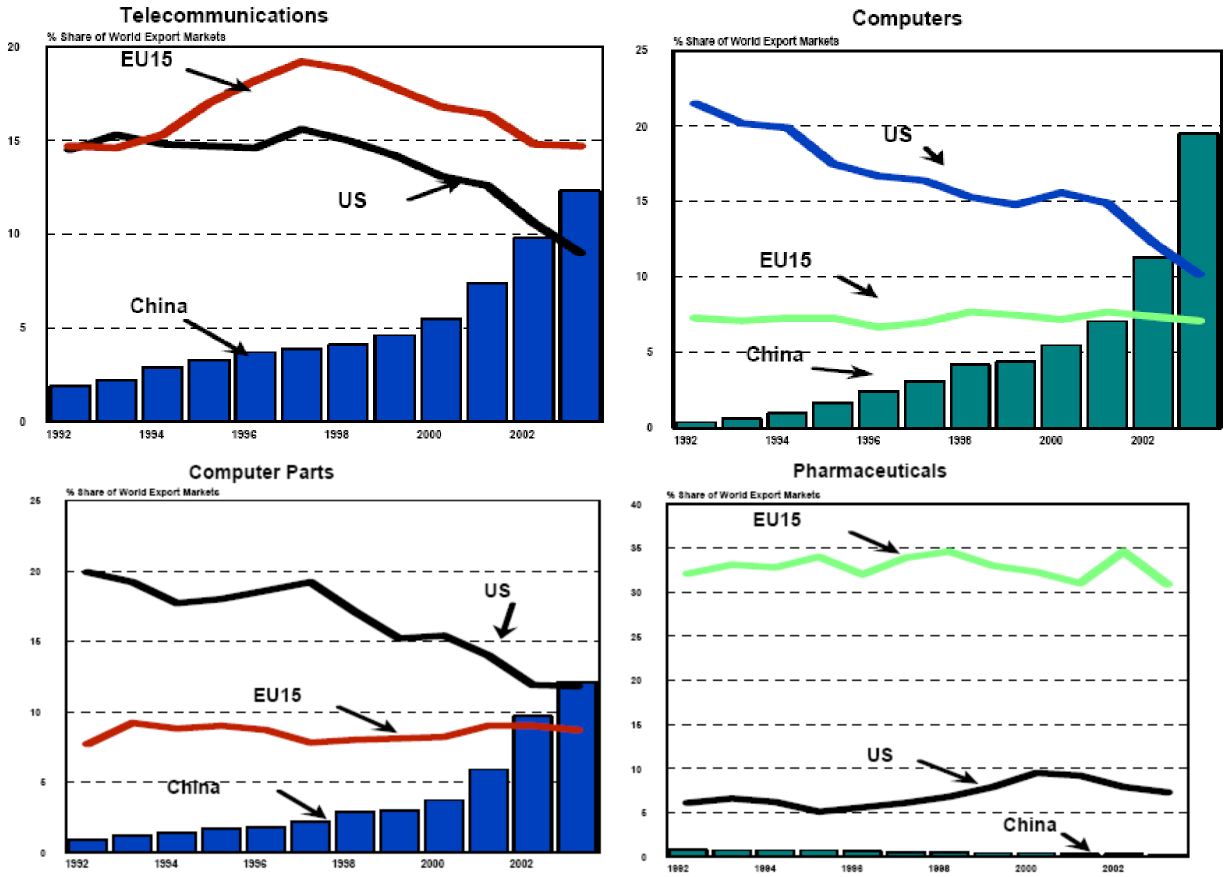
Figures 10 to 13 show how China has succeeded in rapidly gaining market share in a certain number of "key" industrial sectors such as computers, telecommunications, or electronic components, while remaining a long way behind in, for example, pharmaceuticals. What the position will be in a few years' time in a sector such as the automotive industry, which the Chinese government has just decided to make a priority, remains to be seen.

Figure 9: Change in market share of exports of manufactured goods



Source: World Bank.

Figures 10, 11, 12 and 13: Change in China's share of world export markets in certain manufacturing sectors compared to that of Europe and the United States

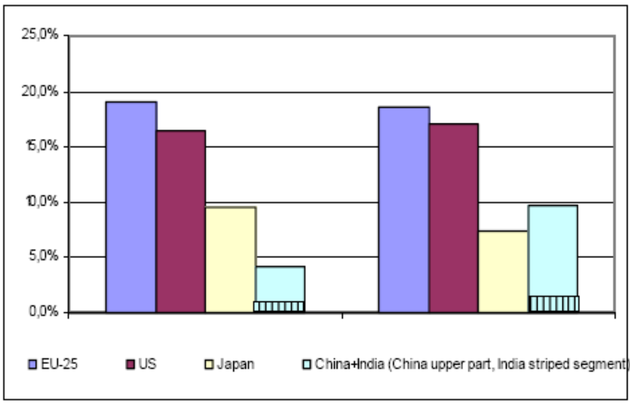


Source: European Commission, DG Ecofin, Economic Papers *"Globalisation: trends, issues and macro implications for the EU» n°* 254, July 2006.

The last very important area is that of the services market, which is often less studied than the other areas even though its share in the economy and in world trade is growing and will continue to grow. This is an area which Europe rightly advocates as a potential response to the loss of market share in a certain number of more traditional sectors.

Figure 14: Variation in share of world trade in goods

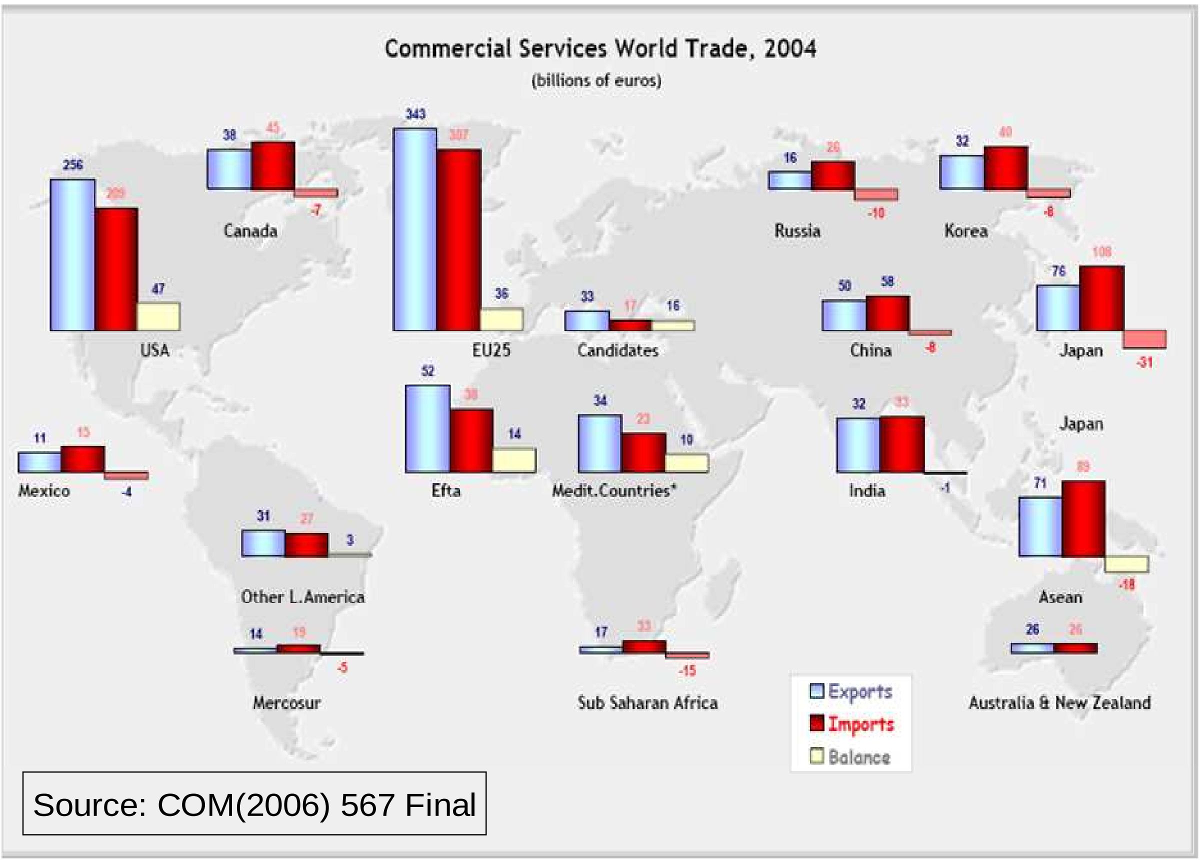
Commerce de bien et services (% des échanges mondiaux)



	1995	2004
EU-25 (excl. intra)	19,1%	18,5%
US	16,5%	17,1%
Japan	9,5%	7,4%
China	3,4%	8,4%
India	0,8%	1,2%

Source: COM(2005) 525 final/2

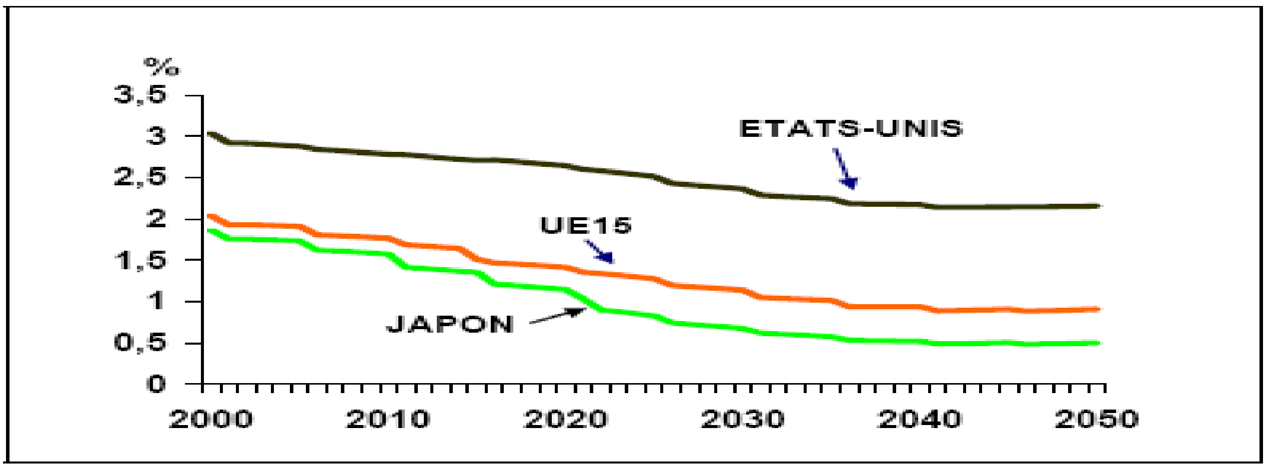
On this point we can do no more than observe a certain erosion of Europe's market share over recent years (a fall of 0.6%) while China and to a lesser extent India are proving to be increasingly important players (an increase in market share from 4.2% to 9.6% in 9 years). However we should not be over-pessimistic; these market shares concern a sector which is expanding rapidly in terms of volume and in which Europe still has a positive trade balance, as the following figure (15) shows.



A5: An ageing European population restricts growth

To this initial economic panorama, we need to add the demographic dimension, which is also crucial for the coming years in view of its strong impact on growth. The European deficit here is clearly visible, in comparison with the slower decline of the United States.

Figure 16: Impact of ageing population on potential growth rates

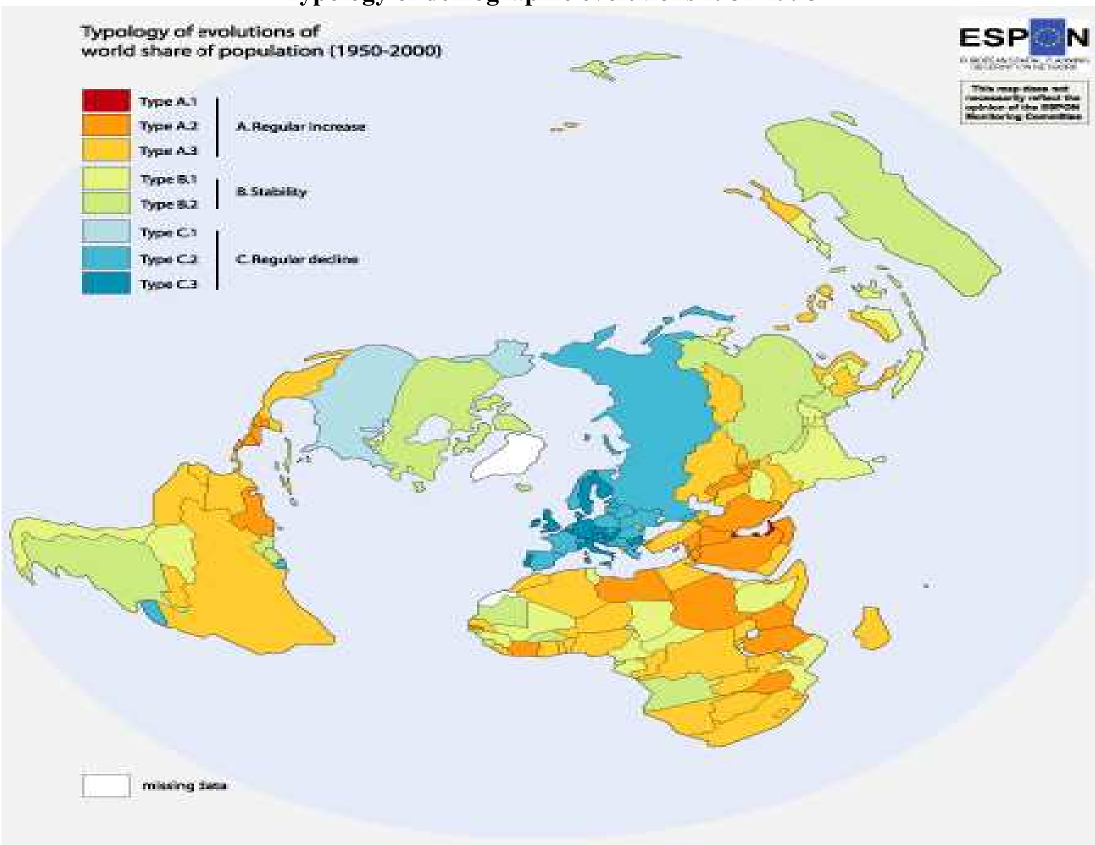


Source: COM (2005) Final/2, Brussels, 03/11/2005

Europe is clearly the ageing continent of the planet. Not a single European country is experiencing the demographic dynamism of, for example Canada or Australia, or even the resistance to decline shown by the United States. Only the situations of Russia, Japan and Uruguay are comparable.

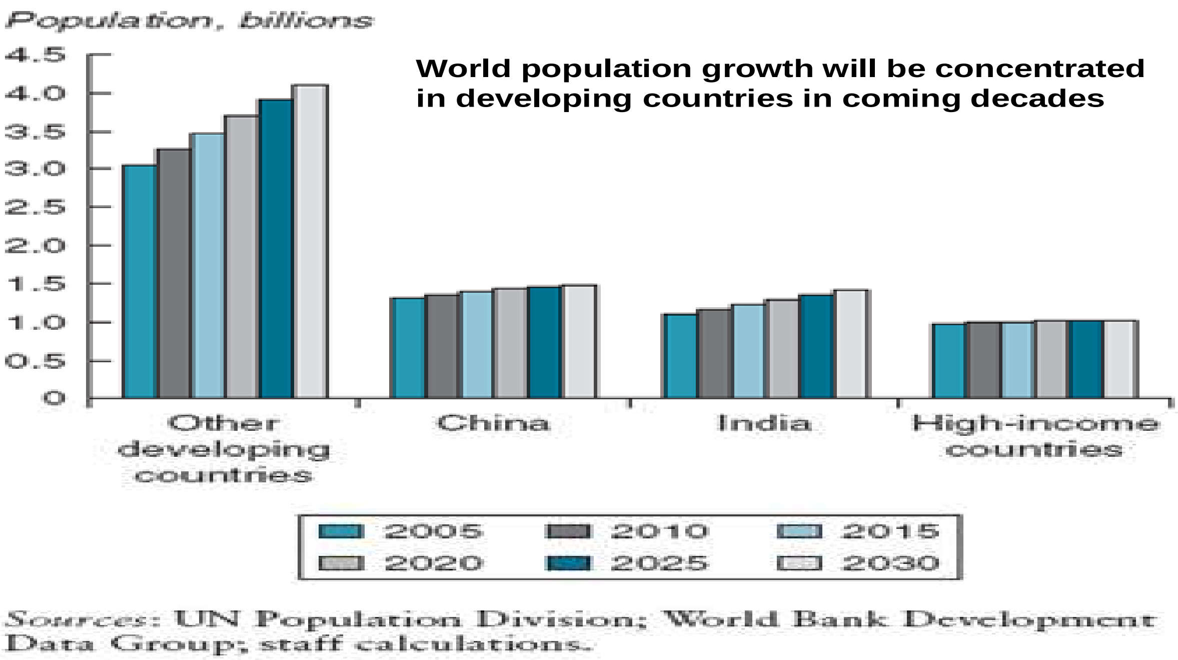
Figure 17: World typology of main demographical evolutions

Typology of demographic evolutions 1952-1998



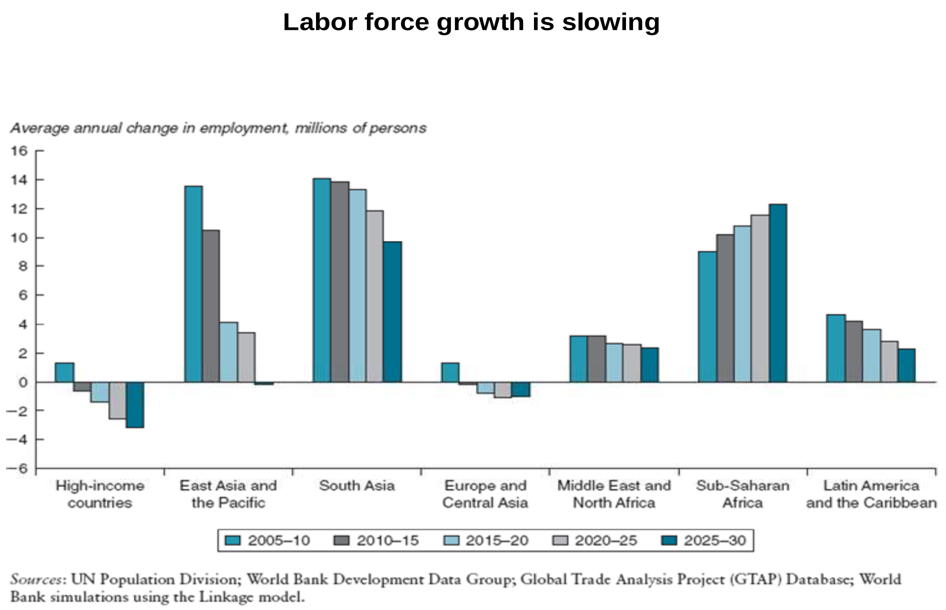
For the most part, in fact, population growth over the next 25 years will be concentrated in the developing countries – precisely those countries in which most of world economic growth will not be concentrated. Population growth in China and India will remain quite moderate in comparison with Africa for example. This leads to a very pessimistic conclusion: average per capita GDP will tend to continue to fall in the planet's poorest countries.

Figure 18: Forecasts for population growth by 2030



These trends will consequently have a major impact on the available economically active population.

Figure 19: Change in employment by major world regions



Only the developed countries and Russia and Central Asia will see a decline in their labour forces. All the other world regions will experience a sharp increase over the next 20 years. This is well-chartered territory in terms of statistical data, since it concerns for the greater part people already born. Two rapid conclusions can be drawn from these observations of population changes:

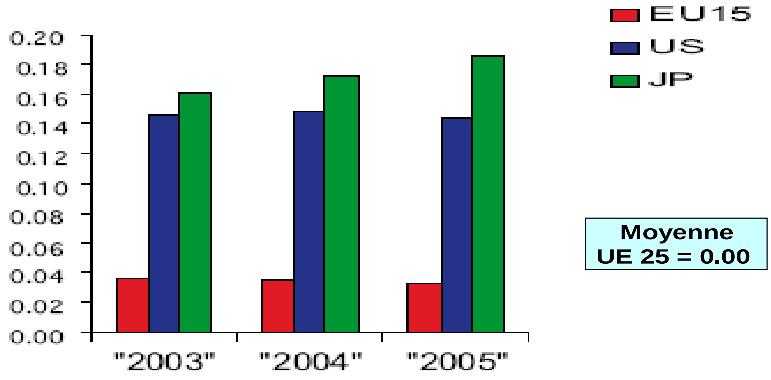
- the high-income countries will need to define a new migration policy so as to be able to respond to future labour market needs;
- heightened international cooperation on development aid is vitally necessary, in view of the very strong negative correlation between economic growth and demographic growth in the low-income countries (especially Africa).

The role that a United – or disunited – Europe could play in relation to these developments remains to be defined.

A6: Innovation is one obvious solution

In this brief panorama of the main economic challenges with which Europe will find itself confronted in the context of globalisation, there remains of course the question of innovation – the key factor in Europe's competitiveness in a global context. Numerous analyses have been made of this question, but forecasting capacity is very limited. We can just about observe, from figure 20, the gap between Europe and its most direct competitors, Japan and the United States.

Figure 20: Comparison of innovation performance of the main high-income groups of countries (Source: European Commission, DG Enterprise and Industry: European Innovation Progress Report 2006)

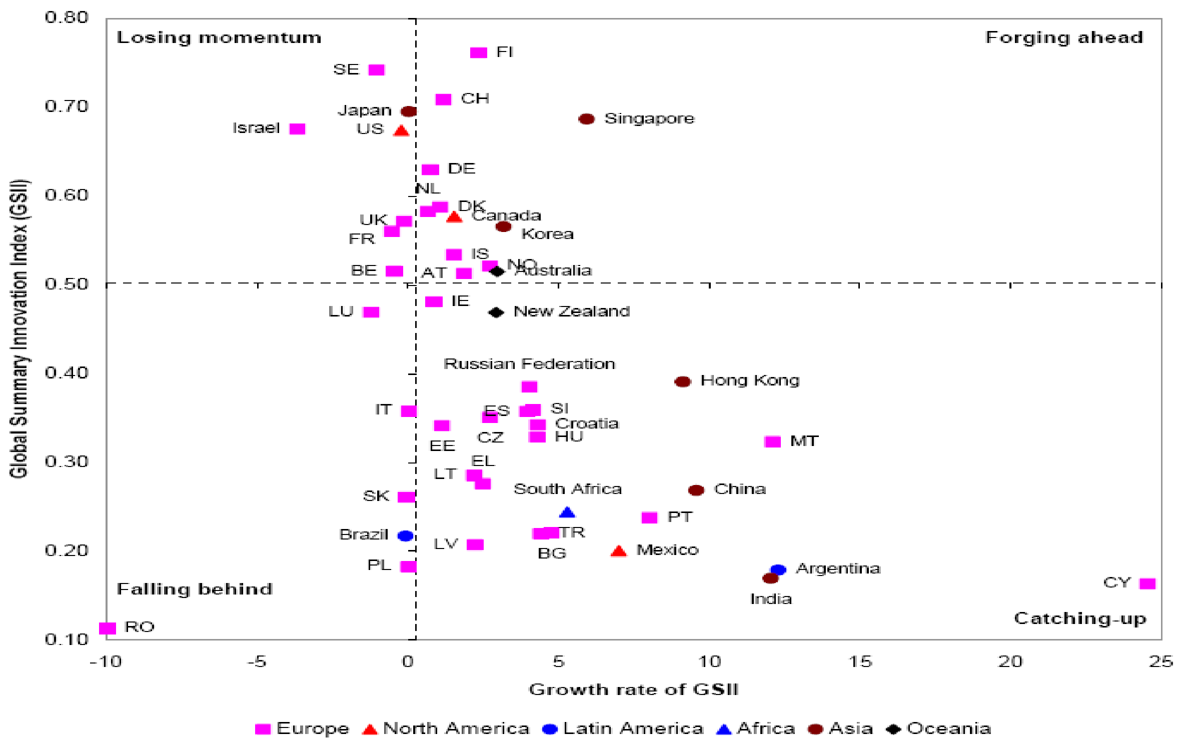


This is without doubt the main challenge for the coming years. Europe has begun, hesitantly, to take this question into account in its policy areas for 2007-2013. From what we can see today, it seems clear that it will have to do so to a much greater extent in the years ahead.

Figure 21 shows the wide diversities among the countries of Europe in innovation performance, whether in terms of levels achieved or dynamism. It is worth noting that the countries that are furthest ahead are not necessarily the most dynamic in terms of change.

Finland is the most remarkable example in this panorama when we consider in particular the numerous development phases it has gone through in less than 10 years.

Figure 21: Comparison of different countries' innovation performance
(Source: Global Innovation Scoreboard Report 2006)



A7: Some initial conclusions

It will of course be necessary to analyse these main overall trends in more detail. Nevertheless they do provide an initial framework for our reflections. Above all, they raise numerous questions about the management of policy priorities, which we will come back to later. Broadly speaking, there are three main challenges:

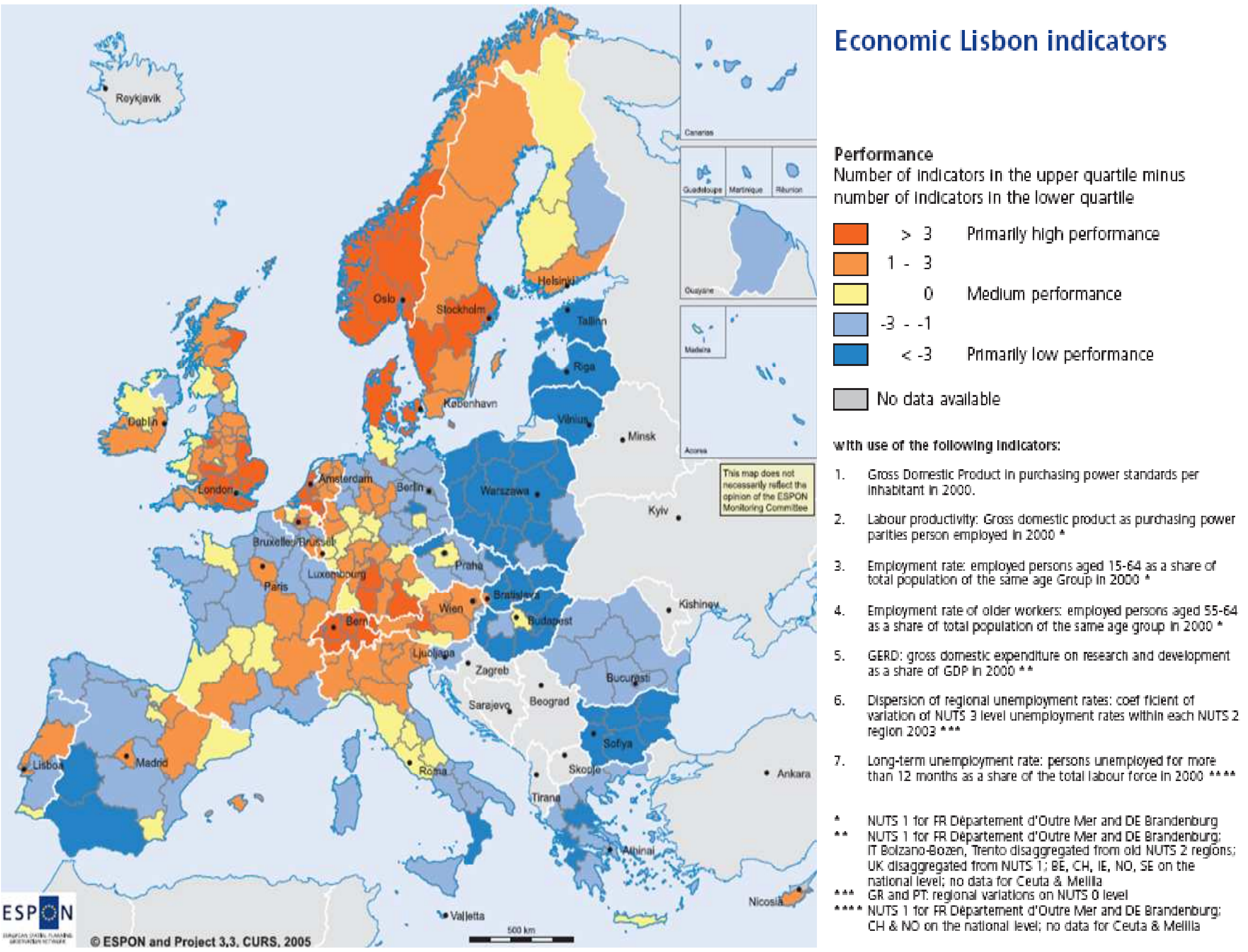
- Europe needs to maintain a high level of economic activity and social protection, thus preserving a clear advantage for its citizens in terms of standard of living, by enhancing its competitiveness in the high value added sectors. For this priority, education and training policy, as well as the type of accompanying economic and social policy, will be the key issue.
- Europe should continue to pursue a policy aiming to achieve a better balance in development opportunities at the level of the planet (the debate on migration will also be important here). As the largest donor of development aid, Europe will no doubt have to strengthen its external policies and specify in more detail what it expects in exchange.
- Europe must as a matter of urgency anticipate and respond to the asymmetrical shocks of globalisation, whether at the level of relations with its citizens or with its regions. The present upheavals are still generating deep-seated changes which we will have to face fearlessly but also without naivety. Not all the European territories will be able to adapt to these changes at the same rate.

It will escape no-one's attention that maintaining an even balance between these three challenges will not be easy. To this already complicated debate we will also have to add the demands of sustainable development, to which we will return later, and which will without doubt make the task of inventing policies for 2014-2020 even more complex.

B. THE REGIONS IN EUROPE

In this section, we will attempt to flesh out point 3 of the above conclusions, i.e. the management of intra-European disparities, which has been one of the key pillars of European construction for many years and which is at the very heart of the concerns of our member regions. The regions are now lucky enough to have at their disposal a wealth of regional studies, compared to the previous negotiating periods, and this helps notably to better highlight the challenges to be addressed. We will limit ourselves here therefore to presenting a few of the most significant illustrations of the problem as it stands today.

Figure 22: The regions and the Lisbon strategy



This first map sums up perfectly the nature of the economic challenges which the European territories are going to have to face. We would have liked to be able to cross-reference these data with a detailed analysis of regional productive systems, but this will no doubt be one of the aims of the ESPON programme for 2007-2013. The present programme does not as yet allow for such detailed analyses (localisation of fragile sectors and, in comparison, flagship sectors of the European economy).

If we compare this first illustration with figure 23, which maps innovation, and with figure 24, which presents the challenges of restructuring, it is easy to see where the challenges facing future regional policy lie. Across the European regions, situations are increasingly diverse, including within each Member State, a phenomenon that is on the increase. The sharpest divisions are no longer necessarily between the centre and the geographically peripheral areas, but rather tend to reflect the different ways in which wealth is created. On the question of innovation, the divisions are mostly between the north on the one hand and the south and east on the other. Concerning restructuring potential, the most dynamic territories are located in a pattern rather like islands of competitiveness corresponding to the large international metropolitan regions which are integrated into global trade flows. The issue is not so much one of a split between the centre and periphery in physical terms, as between territories that are integrated and those that are on the margins of the major trade flows and in terms of industrial and service sector innovation.

Figure 23: The regions and innovation

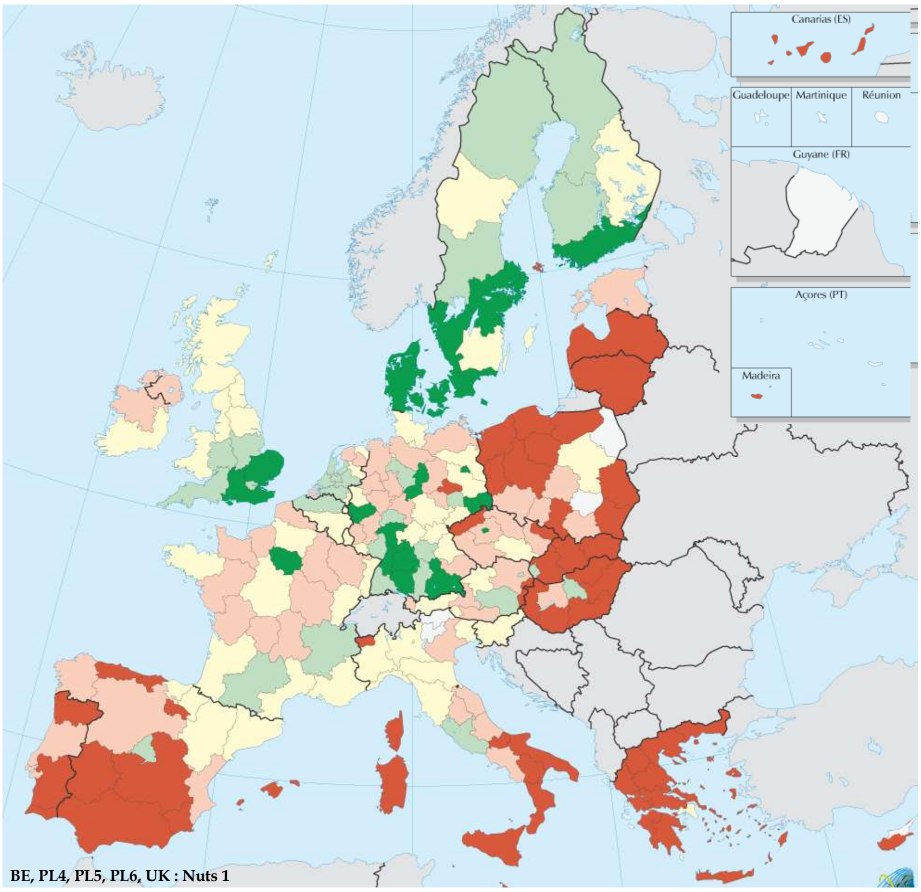
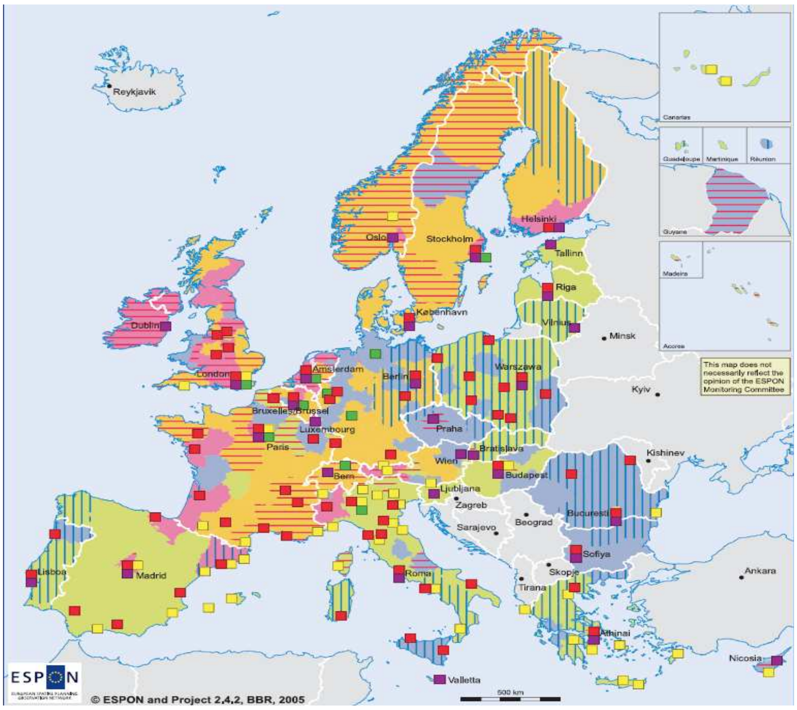
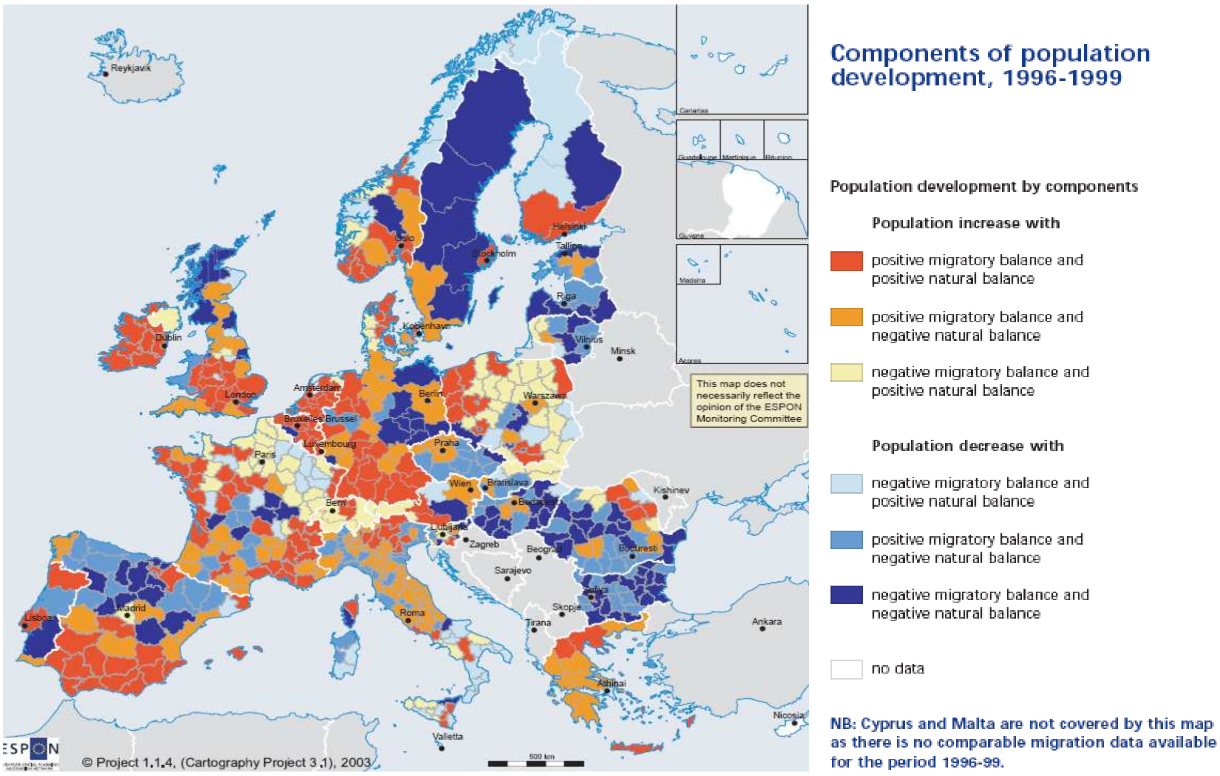


Figure 24: Economic situation and restructuring potential



Concerning the demographic challenges, two observations have to be made:

1. Population development in the European countries is far from being uniform, and it will no doubt be necessary to invent new policies adapted to the nature of the demographic challenges faced by the regions.



2. Interregional and international migration remains at such a low level in Europe that labour market regulation will only be possible by means of a more ambitious regional policy. The risk here of course is that European citizens in those territories that are on the fringes of international competitiveness will re-think their commitment to the European political project – as may also those in the richest territories who are no longer willing to contribute to pan-European solidarity.

Figure 26: Past mobility levels in distance moved, by demographic characteristics

Past mobility level in distance moved, by demographic characteristics (%)

	Within city/town or region	Across regions	Within EU	Outside EU
Total				
EU25	53	18	4	3
EU15	55	19	5	3
NMS	45	9	1	1
Educational level				
Low or none	59	13	4	2
Average	56	17	3	3
High	54	27	7	5
Still studying	17	9	3	1
Employment status				
Working	56	18	4	3
Unemployed	49	16	4	2
Retired	59	20	4	3
Homemaker	56	16	5	2

The first table shows that mobility levels observed as a percentage of the population group concerned are not only very low but mainly concern one particular group – students in higher education. These mobility levels are already low at the intra-national level. On average between 50% and 60% of the population, when mobile, only moves within the same city/town or the same region. In about 20% of cases mobility is between two different regions in the same country, in only 4% or 5% of cases to another EU country, and in 3% of cases outside the EU. It is even possible to conclude that more than 40% of those who have chosen to change their country of residence move outside of the European Union.

If we look at future mobility intentions, the picture is even clearer, since these levels are lower that the actual observed situation. A great majority of European citizens do not want to be mobile, even within their own city/town or region! Even students, retired people or the unemployed do not demonstrate a great desire for change.

Figure 27: Mobility intentions, by demographic characteristics

Mobility intentions, by demographic characteristics (%)

	Within city/town or region	Across regions	Within EU	Outside EU
Total				
EU25	18	7	3	2
EU15	18	7	3	2
NMS	15	4	5	1
Educational level				
Low or none	10	2	1	1
Average	18	6	2	1
High	21	8	4	2
Still studying	34	24	12	6
Employment status				
Working	20	7	3	2
Unemployed	27	11	6	2
Retired	10	2	1	0
Homemaker	13	4	1	1

Note: Figures indicate percentage of respondents who expressed an intention to move in the next five years.
* Married or living together; child = person aged 0–14.

It will be absolutely fundamental to take this point into account in designing tomorrow's policies. There are whole sections of European society on which policies will have no effect whatsoever. Europe will never be the United States. However strong the messages are advocating mobility as the means of regulating the labour market, it is not through mobility but at the level of the regions that this will be achieved.

I.2. THE URGENCY OF SUSTAINABILITY

It is worth reminding ourselves that the promotion of a more sustainable development model at global level, which the United Nations have been calling for since the Rio de Janeiro summit in 1992, requires, first and foremost, action of an exemplary nature. It would be quite illusory to believe that the European States will be able to fulfil the commitments they made at the Rio and Johannesburg "Earth Summits", and to seriously address the Millennium Development Goals, unless they first of all incorporate the requirements of the Gothenburg Strategy into the design of their own policies.

Today, however, the focus is on the so-called Lisbon strategy in favour of competitiveness. If we are not careful, demands for sustainable policies (the Gothenburg Strategy) could become relegated to second place. This is all the more worrying in view of the fact that the state of the environment in general, and that of the coastal areas in particular, is showing worrying signs of a rapid and insufficiently controlled transformation. As the report on "The changing faces of Europe's coastal areas", published by the European Environment Agency in June 2006, highlights:

- transformation of land into artificial surfaces is 30% more rapid in coastal areas than in inland areas;
- movements of population towards the coastal areas is increasing, which is an opportunity for our regions;

- the protection of marine and coastal ecosystems is, in many States, given less attention than that of inland areas even though biodiversity is between five and ten times more varied.

All the forward study analyses agree that the rate of transformation of coastal areas is accelerating and that existing measures to deal with the problems are insufficient. This observation is reinforced by studies on the consequences of climate change, which will bring about profound changes in species distribution and the capacity of different species to resist such changes, as well as the spatial distribution of agricultural production and water resources.

The need for action is all the greater in view of the fact that the possible solutions need to be implemented over a longer timescale than that of the electoral calendar which regulates the life of our democracies. Such solutions require courage. In addition, they call for new methods in policy design and delivery as well as deep-seated changes in behaviour, both at individual and collective level.

Most of these solutions call for integrated policies, enabling all the dimensions of development to be taken into account. For that, we need to review our ways of working, the criteria on which we base the allocation of resources, and the governance of our societies. Such "revolutions" will not take place overnight, and we have had experience, in Europe, of how difficult the implementation of integrated policies can be, with the European strategy for integrated coastal zone management.

The regional level, i.e. regional authorities, have started to react and to organise themselves. The creation in 2002 of the network of regional governments for sustainable development (nrg4SD) is a positive example. This network of regional authorities from the five continents set itself the goal of designing its members' development actions on the basis of sustainable development principles. They have already begun to do this in areas such as water resource management, forestry policy, fair trade, renewable energies and climate change.

The interest shown by the regions of South America, Indonesia and Africa for this initiative demonstrates that it is a promising approach; the time needed to nurture it and develop a real content reflects the difficulties encountered in trying to bring together two diverging worlds. And yet the regional and local level is clearly the most appropriate one at which to give a concrete content to sustainable development. Out of the some 6,000 Agenda 21 that have been adopted worldwide, more than 5,000 are regional or local authority initiatives.

Organising regional capacity to promote sustainable development, adopting a pragmatic and step-by-step approach, setting an example in the conduct of community policies – the best way to export this in development policies - these are the challenges already facing Europe and which will become more pressing in the years ahead.

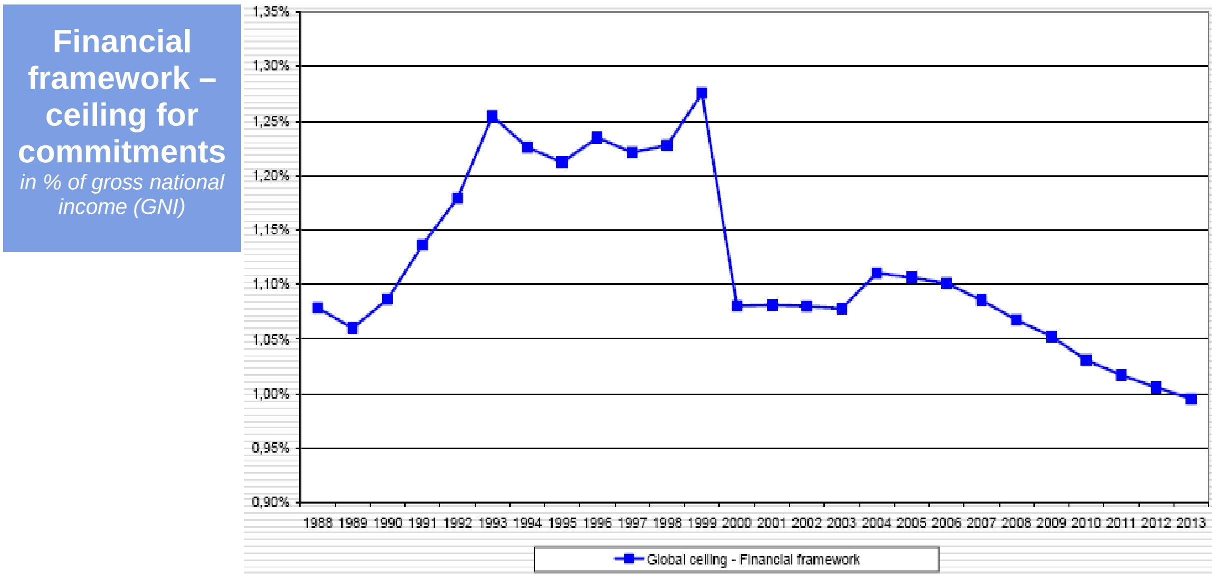
II. EUROPE'S PLACE IN THE WORLD: THREE POLITICAL SCENARIOS FOR A PROJECT

Having set out the framework for the reflections, there now begins a long period of questioning as to how Europeans will take up these new challenges and opportunities, not forgetting that they will not all start off on an equal footing. Will the benefits of the single market, which in stock terms remain extremely high, weigh sufficiently in the political debate when in around 2012 it comes to negotiating the final details of the EU budget for the period after 2013? It is not easy to answer this question today, given the absence of any clear institutional framework. We can just about begin to sketch the shape of three possible political scenarios, which do not necessarily have the same ambition for the future regional policy.

a. "A big step backwards": the trend scenario?

This first scenario has in fact already been outlined by the Member States, when in December 2005 they adopted the financial framework for the period 2007-2013 which we are entering today. It reflects a level of commitment that is lower than that in the years preceding the fall of the iron curtain. We could be tempted to believe that this was not merely a cost-cutting exercise or one of the direct consequences of the failure to ratify the Treaty. It is not unreasonable to suspect that the problem in fact lies deeper.

Figure 28: Ceilings for commitments to the EU budget as a % of gross national income.



Source: DG Budget, European Commission

The question, in fact, since the Berlin Summit in June 1999, when the ceilings for commitments reached 1.27% of Europe's wealth, is not only that of the total amount, but above all that of the acceptable share of total public expenditure that the States wish to actually put in common rather than manage nationally. If we look at how this has changed, it is easy to see that a choice has already been made.

When in 2003 Romano Prodi launched the debate on the budget for 2007-2013, the Sapir report had already laid the foundations for a reflection on the future of Europe in the context of globalisation. The European Commission, with the means at its disposal, provided a satisfactory response, consisting notably of:

- firstly, considerably strengthening the community policies dedicated to competitiveness under chapter 1a of the EU budget. As we know these were subsequently "massacred" by the Council (the European Commission's proposals were slashed by 70%),
- secondly, dedicating an important part of regional policy 2007-2013 to competitiveness and innovation, which remains today without doubt the best decision of that time.

While we can only welcome the brighter fate reserved for regional policy, despite the reserves we could voice today about certain of the procedures for implementing it, what can we say about the European Union's lack of ambition in the face of the challenges we outlined in the first part of this document?

In its Communication of 4 October 2006 entitled "Global Europe: competing in the world", the European Commission concludes by outlining the following measures.

***Internally** we will:*
*- Make sure that **internal policy proposals, while furthering European standards, fit with global competitiveness challenges**.*
*- Make sure the **benefits of trade opening are passed on** to citizens by monitoring developments in import and consumer prices.*
***- Equip people for change** through the new generation of cohesion policy programmes and the European Globalisation Adjustment Fund.*

***Externally** we will:*
*- Maintain our **commitment to the Doha Trade Round** and WTO as the best way of opening and managing world trade.*
*- Make proposals on priorities in trade and investment relations with **China** as part of a broad strategy to build a beneficial and equal partnership.*
*- Launch a second phase of the EU **IPR enforcement** strategy.*
*- Make proposals for a **new generation of carefully selected and prioritised FTAs**.*
*- Make proposals for a **renewed and reinforced market access strategy**.*
*- Propose measures to open **procurement** markets abroad.*
*- Conduct a **review of the effectiveness of our trade-defence instruments**.*

We of course welcome the importance given by the European Commission to cohesion policy to help EU countries adapt to globalisation. However, given the current state of the European project, we have every reason to doubt that the resources and content that will be assigned to this policy will be sufficient, given the extent of the challenges.

- This may be possible in the cohesion countries, given the relative importance of part-financing under the convergence policy.
- In the other regions of the Union, the procedures for implementation and the scale of resources remain well below the level of the challenges the regions will have to face between 2007-2013, even taking account of the necessary earmarking on the Lisbon priorities.

What will the situation be in 2014 if these trends continue unchanged?

- In an optimistic scenario, a regional policy with the same content but after a further cut of one-third in its resources, would attempt:
  - with 5 euros per capita per year to train European workers to adapt to the new international division of production processes, by means of a European Social Fund for adaptation to globalisation which would be ambitious only in name;
  - to make European SME-SMIs innovative in the face of competition from China and India, thanks to the other 5 euros per capita per year remaining in the ERDF kitty.
- In a more pessimistic scenario, the Sapir report would have been right, a programming period ahead of its time, and only those regions lagging behind in development as a result of the most recent enlargements would be covered by a second generation convergence policy negotiated down to a minimum since it would only be defended by a minority of Member States.

b. "Selfisher and selfisher": some conditions for "success"

Even if nobody dares evoke this scenario too openly yet, the risk of a major setback to the construction of Europe can no longer be dismissed. This was the most disastrous scenario sketched out by the European Commission's forward studies unit at the end of the last century when it was commissioned to explore possible futures. Some political indications now give it a certain credibility.

- An almost taboo subject, the first political assessments of the most recent enlargements vary considerably, both in the old and the new Europe. The former reproach the latter for not always playing the game of the single market, while the latter observe with suspicion the desire sometimes expressed for deeper integration, while bemoaning the less advantageous conditions offered to them in comparison with previous enlargements. The atmosphere in the Council's various comitologies are at times tense, and many observers have evoked a certain East-West bipolarity in the debates. Although enlargement has, from an economic point of view, no doubt enabled a large number of jobs to be preserved in Europe, public opinion in the old European countries sometimes tends to blame enlargement for some of the ills arising from globalisation. Today, the term enlargement has almost become a dirty word, and the entry of Bulgaria and Romania to the Union was unfortunately not celebrated – any more than that of the 10 was in 2004 – as grandly as the previous enlargements. Public opinion in some countries remains measured, not to say suspicious, and governments have made little effort to explain to their citizens the mutual benefits of a vast single market of 480 million inhabitants.
- The single global market is still under construction, and the natural tendency to try to make the most of one's assets individually without being burdened by the unnecessary costs of European solidarity is an idea that is gaining some ground. A "miser's Europe" is a real possibility, and with just a few more disagreements it could come closer to reality. Another fact that adds credibility to this scenario is that certain countries that have traditionally been beneficiaries will soon become net contributors to the EU and, in contrast to the preceding periods, contributor countries will now outnumber beneficiary countries. In view of the significant disparities in competitiveness between European countries, the temptation to fall back on an individualist approach could be quite considerable. Are we running the same risk today as in 1973 with the first oil crisis? Could the situation deteriorate so far that we see the *acquis* of the single market being called into question?
- In the current phase of a global opening-up of trade, a natural trend is observable consisting in each European country developing privileged trade relations with areas with which it has long-standing

links – be it the United States, Asia, South America, Russia or Central Asia. An increasing number of bilateral free trade agreements are coming into place worldwide, and some European countries would like to follow this trend, although individually they lack the bargaining power. What will happen if multi-lateral negotiations within the WTO remain at a deadlock and bi-lateral agreements continue to be so successful? Comparative trade advantage with the rest of the world is even sometimes becoming a source of competition between Europeans, but is something that can only be modulated by the interdependence of the large industrial and commercial groups. In parallel, the euro zone is barely creeping along, and some observers have no hesitation in blaming the single currency for the low level of European growth.

- Will European solidarity suffer the same fate as the gap between the resources promised to achieve the millennium goals, when we can see the difficulties the States have in respecting the commitments they made?
- A final point, there are no indications today of a positive outcome following the failures of the French and Dutch referendum. The risk that the scepticism that was expressed on those occasions could spread to public opinion in other European countries is not to be taken lightly, all the more so since a number of controversial issues between Member States have been highlighted in the media: the conflict in Iraq, energy choices and immigration policy in particular. Rising nationalism as an easy solution to the difficulties in confronting a new world is not to be dismissed. Historically, this scenario is no novelty. It has always led to war.

In such a scenario, we could easily imagine an EU budget transformed into a major "phasing out", keeping a few symbolic and inexpensive policies to continue to create an illusion. It goes without saying that if this scenario were to supplant the preceding one, then regional policy would be no more than a distant memory. The only remains of a bygone age would be a few discounted "cohesion fund" cheques, paid out to the poorest European Member States. A few speeches on the virtues of an intergovernmental approach would just about keep the European myth alive.

c. "A renewed vision of Europe's place in the world": laying the foundations for political reconstruction

Building a new political project around a vision of Europe's place in the world is without doubt the noblest of tasks for the heads of state and government since the end of last world war and the beginning of European reunification. It is often in times of adversity that the most just causes are born, and those which hold out the greatest promise for the future.

Europe is not in danger from a macro-economic point of view in the context of globalisation, but it will have to face two major challenges in order to preserve its unity and its international presence:

- to prepare for and adapt to the future, while maintaining its social cohesion. Not all Europeans will be competitive in a situation of heightened international competition, and it would be illusory to believe they could be. But each and every European citizen should have the possibility of being part of this new, profoundly changing model of society;
- to maintain its territorial cohesion through equity in its policies and a closer involvement of its territories and of the whole range of political forces that are at work in them. Europe has a model of citizenship and democracy that should be preserved and promoted. In order to go further and transmit these values in a united manner in this new world, Europe will have to stabilise its own model internally and overcome its principle contradictions.

Europe has very nearly achieved **economic cohesion** thanks to:

- a trade policy with which it can advance as a united front in the WTO;
- a strong euro which protects it from the trials of the past and which wants nothing more than to be extended to the whole of the EU;
- a competition policy which is beginning to adapt itself to the challenges of globalisation by focusing more on economic activities anchored in the territories;
- the beginnings of a greater focusing of all its policies on innovation, in order to develop its assets on the world stage;
- a single market of 480 million consumers, the positive effects of which for our economies and on employment have been under-estimated.

- In addition, unemployment will soon become a less serious problem in Europe simply for demographic reasons, although it will still be important to tackle its essential cause, which is workers' adaptability to the new challenges.

What is probably lacking to enable Europe to go further is:

- the launch of a real European fiscal policy. For this to be credible, however, greater harmonisation of the main national budgetary aggregates will be necessary, the most important of which are public borrowing and public deficits. All the Member States are now tackling this question very seriously and we can be reasonably confident that they will achieve this objective before 2014.
- A gradual move towards direct taxation to finance the European budget. This would allow for a more ambitious policy. There are seven years remaining in which to see what is still a dream become a reality.

These two conditions for taking European economic integration further are not insurmountable. To be credible, they will need to be supported by a deepening of the two other pillars of European cohesion, i.e. **social cohesion and territorial cohesion.** It is around a win-win pact between the European countries and with all the citizens of Europe that the EU can find a new unity. These steps forward will only be possible within a renewed institutional framework that reflects the multi-level governance that will have to be accepted inside the Union.

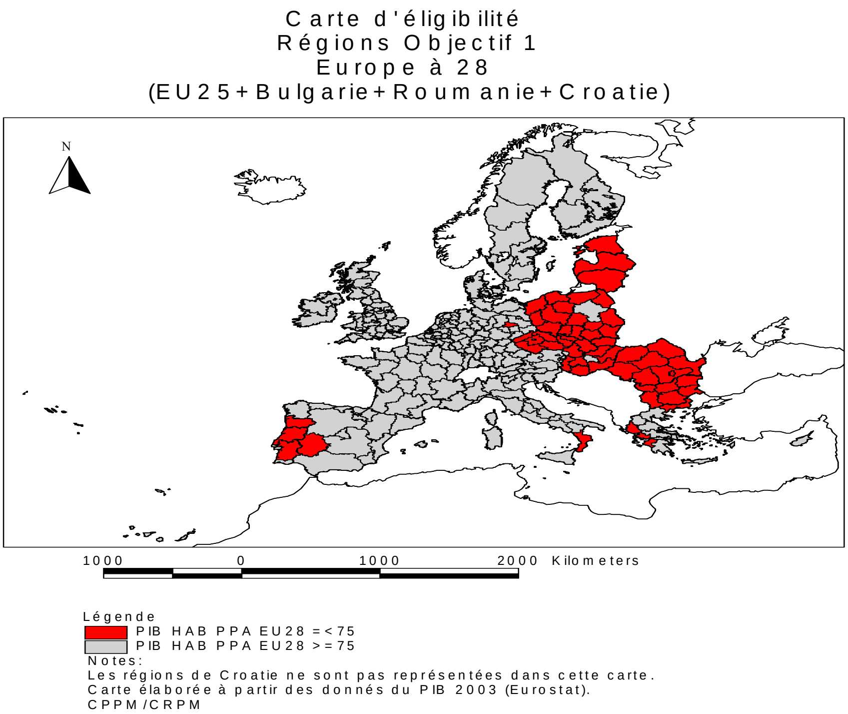
We will attempt in the third section of this document to outline the major role that the regions and their territories will have to play in this scenario, notably in the matter of territorial cohesion, given that the social chapter is today in a majority of countries a national competence.

III. WHAT POLICIES WILL THE EUROPEAN REGIONS NEED TO SUPPORT THEM ON THE WORLD STAGE?: THE MAIN CONDITIONS FOR SUCCESS

a. What kind of territories will we see in 2014?

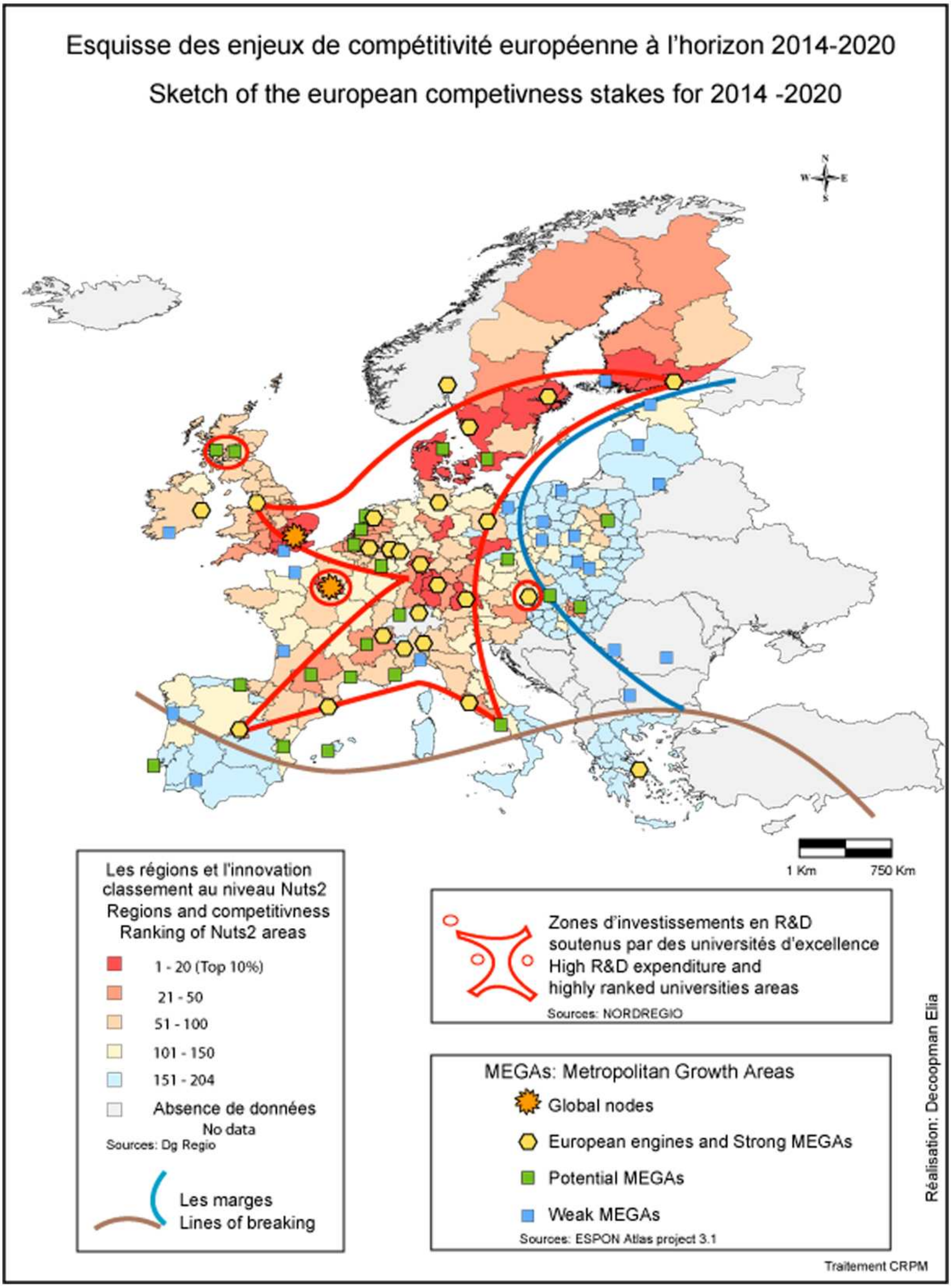
If the reform of the future regional policy were to be prepared according to the same procedures as in the past, the discussions would be launched on the following basis. In the future eligibility map for 2014-2020, Germany, Spain, Italy and Greece would hardly be concerned by the convergence objective, which would be limited to the East of Europe, Portugal and two outermost regions. The question would be, what kind of policies could be implemented in a coordinated manner under the regional competitiveness and employment objective, using resources that would be even more diluted than they are today because of a sharp increase in the eligible population.

Figure 29: Map showing regions eligible under the convergence objective on the basis of 2003 per capita GDP levels



The summary map offers a much wider panorama of the territorial challenges facing Europe and the necessary adaptations to global challenges that each of the territories will have to make.

Figure 30



These territories will all have different needs, linked notably to:

- their region's demography;
- the skills of their economically active population;
- the nature of the economic sectors in which they have been successful – or not – in developing a certain excellence at global level (agriculture, tourism, services with varying degrees of value added, industrial activities);
- their research capacities;
- the quality of innovative spirit that they will have been able to foster and support in their territories;
- the nature of their population settlement, ranging from sparsely populated rural areas to metropolitan regions;
- the capacities they will have developed for relations with non-EU countries on the basis of their specific characteristics;
- the economic exploitation of their natural and environmental assets or heritage.
- etc.

Because of this, they will all require specific contractual arrangements, in line with the values of the European project. This will call for a completely new approach to regional policy, in terms of the content of the actions, governance of the policy, as well as its funding.

b. A new governance for the regions, actors of globalisation

The management of regional policy on the basis of a contract between the EU and the Member States is now a thing of the past. Effective, efficient, modern and reactive public action can no longer be hampered by unnecessarily complex and technocratic mechanisms at the level of decision-making and funding.

Future generations of programmes must – on the basis of a community framework negotiated between the European Commission, Member States, and the regions – be implemented individually for each of the regions according to their specific needs. This is the price Europe must pay to regain credibility in the eyes of its citizens. There would be nothing to stop Member States acting in close partnership with their regions and subsequently contributing additional or complementary funding to the public policies to be implemented. This should be possible in the framework of a flexible three-party contract which can be adapted to the reactivity needs of public action in the face of the rapid changes related to globalisation. Firms and their employees are nowadays required to be reactive to change; the same demand should be made of the policies that are intended to support them. Regional authorities should be given more responsibility, in close partnership with their public, private and territorial partners, as is the case in any advanced democracy. The evaluations we have conducted on the implementation of regional policy in 2007-2013 show that there is still a great deal of progress to be made in this field.

This new regional policy must also be clearer, more visible and must avoid setting itself a vast number of ambitious objectives that it will never be able to achieve outside the convergence regions. The one priority should be to prepare workers and social and economic players for the new challenges linked to globalisation. This will include:

- continuing training for workers, with assistance from a regional policy for employment which will both anticipate and react to needs (national educational policies will be crucial as well, notably in the south of Europe);
- support for the productive fabric, boosting innovation and presence on the European and world stage. Consideration should be given to extending this to certain services sectors and agriculture, including notably the "economic diversification" strand of rural development policies;
- bringing the territories up to standard in terms of the challenges of globalisation, notably in terms of research, information technology, and strategic economic monitoring in general.

In addition, in order to give this regional policy greater effectiveness and visibility, the following points will be important:

- it should focus exclusively on the mission of training workers and adapting the regional economy to globalisation, and should be implemented in close partnership with all representatives of economic life and civil society;
- the programming methods will need to be completely revised to involve all stakeholders right from the design stage, in order to achieve a better mutual understanding of what is at stake;

- much greater attention should be given to communicating on the role of each partner in this programming process and on the added value contributed by the EU, rather than to the administrative burden that weighs on its design and delivery today;
- use of the policy should be further simplified, by means of a single fund for regional development and adaptation to globalisation;
- partnership working should be given greater scope and responsibility to achieve the basic objectives, while preserving a certain flexibility in defining regional budget allocations;
- the amounts of funding allocated per region should be considerably increased. It would still however be possible to use a system of allocating funding proportional to the scale of the adaptations to be made, the wealth of the region and its tax potential. If such a system were designed in a sufficiently fair and equitable manner, we would no longer even need to make any differentiation between convergence regions and other regions. A well designed system of funding allocation, with progressive and equitable thresholds, would thus eliminate:
    - "threshold effects";
    - statistical effects;
    - phasing in and phasing out.
- Such a configuration would make it much easier to present the virtues of the European model to our citizens in a manner that is simple and clear to everyone.
- Such a policy, incorporating rural development policies that will have to prepare the rural areas for the new challenges of globalisation, would have to be financed at the very minimum by a budget equivalent to 0.60% of European wealth (equivalent to the current heading 1b + rural development, plus an additional regional contribution from research and innovation policies).

c. Towards a real delivery of certain major European sectoral policies

Implementing policies on sustainable development, transport or sustainable energies through the prism of regional policy does not work, or rather no longer works. There are numerous reasons for this, of which the following are only the main ones:
- most of these policies come under the sovereign competence of national governments and are not shared with the regional level;
- the budgets for regional policy, apart from convergence, are too small to have any real impact;
- the quite praiseworthy political objectives are swamped by the complexity of the decision-making and programming mechanisms;
- the political importance of sustainable development and the Gothenburg strategy has for example been completely swamped by earmarking in favour of the Lisbon strategy and in the different programming phases, to such an extent that it is impossible today to measure the actual extent to which they are taken into account;
- interregional governance of these policies, which is often necessary, as for example in the case of transport, does not work most of the time;
- it is far from certain that complementarities with national and community policies actually exist (notably between the TEN-T, transnational cooperation, national and regional programming to take just one example);
- the principle that sectoral policies should comply with the criteria of economic and social cohesion is no longer applied;
- etc.

And yet local and regional authorities play a major role in the delivery of these policies, often in complement to other sources of funding, both public and private. The question thus remains, how can we identify the means through which it will be possible to give a really new impetus to these policies at European level?

In our view a number of ideas should be explored:

1°) Give a new political visibility to a transport policy, a policy for the environment and for adaptation to climate change, and an energy policy, that will have real community competence. For the time being:
- there is no common transport policy, and the TEN-T budget remains purely symbolic in relation to the ambitions it displays;

- an environment policy exists, essentially devoted to regulatory aspects but with no budget, or nearly no budget, available for applying this;
- there is no European energy policy, not even for sustainable energies, even though this is a vital question that concerns all European citizens and will impact heavily on their future.

In our view these three policy areas are sufficiently important to merit particular attention in any review of the constitutional treaty. It would be surprising if European citizens were to be strongly opposed to such a proposal.

2°) Linked to the preceding point, a new budgetary visibility should be given to these policies, which at present are swamped by complex budget headings indecipherable to any layperson. If the European Council or certain of its members raise objections to the Commission's financial proposals in favour of sustainable development, they should be able to assume their position politically in front of public opinion.

3°) All levels of public action – national government, regional and local authorities – should be more involved, by means of three- or four-party delivery procedures negotiated at community level on the basis of calls for projects or regionalised priorities defined in partnership.

4°) Finally allocate regionalised objectives at European level with the necessary level of funding for their delivery:

- an example to illustrate this point would be a European maritime policy which would set objectives such as the cleaning-up of the Mediterranean or the Baltic Sea, bringing together around the same table all the players concerned and proposing an EU financial contribution;
- in the same way, we could imagine a number of priority corridors, either land-based or maritime, being adopted on the basis of genuine negotiations between all the players concerned and not merely the adding together of different national priorities, as is the case today. Such corridors should comply with stringent sustainable development standards, which would permit specific authorisations in terms of derogations from DG Competition;
- part-funding could also be made possible under the heading of promotion of sustainable alternative energies, for which numerous players could be eligible, in particular local and regional authorities;
- etc.

Using mechanisms such as these, European action can be made much more visible and efficient and brought closer to the concerns and motivations of Europe's citizens.

d. Towards a real EU territorial agenda

In many policy areas a territorial approach can give new and real meaning to the European project, whether in helping Europeans adapt to globalisation, in programming a certain number of major sectoral policies, or in promoting European democracy as a model outside our borders as is envisaged under the Union's external policies in the programming period 2008-2013. It is an approach based essentially on the need to find a new and closer link with the citizens of Europe, through a more effective involvement and greater responsibility being given than in the past to the sub-national tiers of democratic government, in which the regions have a real role to play as a driving force in their territory. When we evoke the idea of a territorial agenda for Europe, it is essentially this idea to which we are attached.

Ministers in charge of territorial development policies have reached similar conclusions to ours, which they will share at a seminar in Leipzig in May this year. We agree with their conclusions to a large extent when they highlight the importance of having greater recourse to territorial approaches in the context of globalisation in order to strengthen the governance of the Union's policies.

On the other hand, we have problems sharing their conclusions on the nature and mechanisms proposed for action. It is, in our view, difficult, in a Europe of 28, to believe in the virtue of purely inter-governmental approaches, which flout:

- on the one hand genuinely regionalised approaches involving, in terms of governance, all the territorial tiers;
- on the other hand any clearly expressed European mechanism for cohesion between territories.

It is not enough to share objectives; it is also necessary to share common and communitised instruments and mechanisms. The CPMR has always viewed the concept of "territorial cohesion" as a cross between the value of multi-level governance and the value of solidarity between territories. It is concerned that this vision, fiercely defended during the consultation on the convention on the future of Europe, is sometimes deliberately misinterpreted in favour of a purely inter-governmental approach by administrations in charge of territorial development seeking to use regional policy as a tool aimed above all at financing their national territorial policies. It would in our view be a serious mistake to go down this road, and would certainly not be in the interest of the fundamental issues, on which we broadly share the same point of view.

However, there are many new ideas worth pursuing between now and 2014 to flesh out all these concerns. This should be done at the highest decision-making level.

Conclusion

This exploration of a possible future for regional policy after 2013 is, for the CPMR, only the first step in a year 2007 which will be devoted to the future of post-2013 policies. We intend:

- firstly, to complete it in the light of the development of the debates on the future of the constitutional treaty. It is clear that the results of the current negotiation and the follow-up that will be given to it in the countries which have not ratified the draft treaty will have a major impact on the credibility of the scenarios and options proposed;
- secondly, to add input from a reflection on developments relating to the other main components of the EU budget, and notably policies which traditionally have a strong territorial impact (CAP and rural development, transport, environment, research, etc.).

It also needs the addition of a political perspective concerning the necessary balance between the Lisbon and Gothenburg strategies, currently the two cornerstones of the Council's strategy.

This first basis for reflections, debated by our Political Bureau, enriched by European Commission's publication of the 4th Report on Economic and Social Cohesion in the spring, will be further developed with a view to its presentation as a political proposal at the meetings of our policy-making bodies in June (Political Bureau) and October (General Assembly).

Seminar
The EU Budget: What for ?

Session V
The EU budgetary procedure
Alfredo DE FEO

The questions raised

- Should the time frame of the financial perspectives be shortened ?
- Should it be synchronized with the European Parliament elections ?
- Is there a need to increase the flexibility in budget allocation ?
- Should there be a mid-term review every 3 years, or regular annual revisions of the expenditure allocations?
- Is the existing division of competences between the European Council, the European Parliament and the European Commission appropriate ?
- What reforms could be envisaged to better coordinate EU, national and sub-national budgetary decisions ?

Aim of the introduction

- Is to offer some elements for reflection to open the debate:
  - Evolution over the last two decades
  - Lessons to learn and some reflection for the future

The modifications since 1988
(the first Financial Perspective)

- Evolution of the legislative procedure
- The evolution of financial perspectives
- The evolution of the annual budgetary procedure

Evolution of the legislative procedure

- the legislative decision making: **CODECISION**;
- **EP: More** involvement in the legislative procedure
- **EP Less** margin of manoeuvre in the budgetary procedure

Consequences

- **BEFORE 1995**:
  - EP free to set the amounts for the programs in the annual budget according annual political priorities
- **AFTER 1995**:
  - Respect of the financial envelop when co-decided, otherwise free ;

More rigidity

- the 7-year programs secure the financing but lose the political priority;
- The IIA of April 2006 addresses the problem introducing a 5% flexibility;
- Partial but positive answer;

The evolution of financial perspectives

- The two Delors packages: increase of own resources during the period;
- Agenda 2000: stagnation;
- Prodi package: reduction of resources

The evolution of the annual budgetary procedure

- **The procedure has evolved since 1975** :
  - Calendar more time for each Institution
  - Maximum Rate of increase of NCE replaced by the respect of the ceilings
  - Reinforced the co-decision element
- **The Budgetary negotiations concentrated** :
  - Financing of the new initiatives and priorities within the ceiling
  - The mobilisation of the flexibility instrument;

Lessons to learn: concerning the MFF

- The MFF in the Constitution/Treaty is a progress for the European Union;
- The abolition of classification reinforces the co-decision nature of the budgetary procedure:
  - The transformation of Council's 2nd reading in a „common position" doesn't simplify the procedure
  - the trigger mechanism: guarantees the negotiation dynamics

Lessons to learn: concerning the MFF

- Duration synchronised on the timeframe of the Institutions (EP proposal):
  - Five years duration
  - Proposals and adoption linked to the Institutional calendar
- Reinforce the follow up of the financial programming;

Lessons to learn: concerning the legislative programs

- The duration of legislative programs should not be linked to the MFF;
- Legislation should be adapted/modified/discontinued when necessary not every 5/7 years;
- No more confusion between legislation and financial resources
- the financial envelop should be defined by the budgetary authority in the MFF decision

Lessons to learn: concerning the annual procedure

- Budgetary authority more focused on
  - monitoring the quality of the implementation;
  - the use of the margins;
  - Simplify the procedure (1 reading and conciliation then mechanism III-310)
  - the financial programming.

Conclusion

- The revision of the budgetary procedure is part of a review process;
- The budgetary procedure should increase the flexibility;
- The MFF should foresee an effective updating/revision mechanism;
- The legislative and budgetary procedure should be indipendent;
- The budgetary procedure should be simplified;

I hope there will be enough elements to open a debate

Thank you

A European Tax?

By Daniel Gros,
CEPS

Abstract

The contribution focuses exclusively on the revenue side of the EU budget. It argues that it would be desirable to make the financing of the EU's budget independent of contributions from national treasuries. This could be achieved through a European VAT surcharge, of around 1.5 % points. European citizens could then see the cost of Europe directly on their shopping bills and negotiations about the financing of the EU's budget could concentrate on one simple number, namely the percentage of VAT that should be devoted to the EU.

Prepared for
Notre Europe Seminar
The EU Budget: What for
Brussels, April 19th, 2007

A European Tax?[1]

1) The present resources of the EU

At present the budget of the Union has three main 'resources' i) custom and agricultural levies (traditional resources), ii) a VAT resource levied on a 'notional' harmonised VAT base,[2] and, iii) a resource based on gross national income (GNI). The latter plays a residual role: its amount is determined ex-post so as to fill the gap between actual spending and the revenues flowing from the traditional and VAT resources. This residual is then allocated amongst the member states in proportion to their share in the Union's GNI, and is paid by each member state out of its national budget. As may be seen from Table 1, over the last ten years this GNI resource has come to represent three-quarters of total revenues.

The fact that the GNI resource dominates revenues is in flat contradiction with the EC Treaty. Art. 269 prescribes that "the Union shall be financed wholly from own resources". By contrast, under the present system the vast majority of Union resources comes from well-identified contributions from national budgets, which the member states inevitably consider 'their money' and want to compare with 'their' receipts from the EU budget.

Table 1. EU-15 own resources, 1996-2005

Percentage share of revenues:	1996	2000	2005
Traditional	19.1	17.4	11.4
VAT	51.3	39.9	14.1
GNP/GNI	29.6	42.7	74.5
Total own resources (€ billion)	71.1	88	108.5

Source: European Commission.

2) Incentives to maximise 'juste retour'

For any individual member country, the return from defending an EU-wide, encompassing interest is dwarfed by the advantage it can obtain from a change in the budget in its own favour, even if this leads to lower overall efficiency. This perverse incentive structure applies even to the largest member country, Germany, which accounts for a little less than a quarter of the budget and EU population. For Germany the return from spending efficiently one euro on some EU-wide interest would be around 25 cents, only a quarter of the return of any one euro spent in Germany. Thus, if the German government has the choice between more spending on a European public good and more

[1] Based on section 3 of Gros, Daniel and Stefano Micossi (2005) "A Better Budget for the European Union More Value for Money - More Money for Value" Policy Brief No. 66, Centre for European Policy Studies, CEPS, Brussels.

[2] The base is calculated on the basis of national VAT receipts and capped at 50% of each member GNI so as to correct for the allegedly regressive nature of VAT. In practice, when capping applies, this resource is turned de facto into a GNI-based resource. Since 2002 the VAT call rate for the Union is 0.5%.

spending on something that mainly benefits German interests, it will always chose the latter.

The same reasoning applies with even more force to the other member countries whose stake in the EU budget is smaller. Moreover, the problem grows with each successive enlargement because each time the stakes of individual member countries in the budget become smaller and smaller. For example, the largest new member country, Poland, has a share in the EU budget of less than 5% and a population share below 10%.

Therefore, it is not surprising that the new member countries (like the old) concentrate their efforts in diverting EU transfers to their own citizens while preserving the present budget structure.[3] The skewed distribution of payments to the member states under the CAP and the structural fund programmes only aggravates the problem.

The problem was aggravated in the 1980s by the decision to grant the United Kingdom a 'rebate' in order to correct an otherwise unbearably large net contribution by that country, which has a small agricultural sector and displays limited eligibility for structural support. The UK rebate and the bitter negotiations that preceded it strengthened the perception of the EU budget as a vehicle for intergovernmental transfers, reflecting countries' negotiating strength. Over time, the fairness of the rebate has come under increasing criticism, since other member states with lower per capita income display higher net payments to the EU budget, as a ratio to their GNI. But the present contribution will not discuss this issue.

3) De-linking the EU budget from national treasuries: a VAT surcharge

Changing this state of affairs requires that on the revenue side the direct link between national treasuries and the EU budget be rescinded, and the cost of Europe be made to fall directly and visibly on the citizens of the Union.

However, we must also bear in mind that, under Art. 10 of the EC Treaty, Community programmes and activities within the border of the member states are implemented by their public administrations. It is not possible, nor indeed desirable, to create a separate EU tax administration.

Therefore, the solution would be to rely on national tax systems and 'dedicate' to Europe the revenue from one particular tax. Efficiency and equity require that this tax be levied on a broad base, harmonised at EU level, at a moderate rate. A broad base also entails that special allowances on grounds of horizontal equity can be kept to a minimum, as the overall burden would continue to amount to a small share of GDP/GNI.

Since the aim is to make the cost of the EU as transparent as possible to European citizens, it is tempting to jump to the conclusion that the best way to achieve this is to add a 'Euro tax' to the personal income tax return bill that most citizens have to fill every

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[3] The political importance of the contribution to the EU is heightened in countries with a federal fiscal system. For example, in Germany the revenues of the federal government amount only to around 20% of GDP. This implies that a contribution to the EU equivalent to 1% of GDP accounts for 5% of the revenues of the federal government in Germany. In other countries where the revenues of the central government are a much higher proportion of GDP, the relative importance of the contribution to the EU budget for the central governments is smaller, even with similar contributions to the EU budget as a share of GDP.

year. However, this solution is not feasible in practice since it would lead to a highly unequal distribution of the burden, given the large differences in the national definitions of taxable income. As a result, the yield of personal income taxation varies widely across member countries, with low values around 3-4% of GDP (e.g. Slovakia and Poland) and peaks over 25% of GDP (e.g. Denmark).

Narrowness and lack of harmonisation of the base also seem to rule out, as feasible alternative, a surcharge on corporate income. The proposal of taking the money for the EU from central bank reserves does not meet the test of visibility and accountability vis-à-vis European citizens. Moreover, the yield would only cover a fraction of the budget of the EU as long as price stability is maintained.

Most of these difficulties do not arise with the VAT. Its base has been reasonably harmonised; the rates do not differ as greatly as do those for personal income taxation; the differences in yields are relatively minor, ranging from a low around 6% of GDP in countries like Italy and Spain to a maximum of 9% of GDP in Hungary and Sweden (see Table 2).

Table 2. Private consumption and VAT (% of GDP, 2003)

	Private consumption /GDP	VAT/GDP
EU-25	58.3	7.0
EU-15	58.2	7.0
Belgium	54.5	7.0
Czech Republic	50.9	6.5
Denmark	47.2	9.7
Germany	59.0	6.5
Estonia	56.6	8.9
Greece	67.2	7.8
Spain	57.8	6.3
France	55.5	7.2
Ireland	45.2	7.2
Italy	60.4	6.1
Latvia	63.0	7.3
Lithuania	64.9	6.9
Luxembourg	41.9	6.5
Hungary	54.7	9.1
Malta	60.8	7.1
The Netherlands	48.4	7.7
Austria	56.1	7.9
Poland	66.0	8.2
Portugal	62.3	8.5
Slovenia	54.4	8.9
Slovakia	55.3	6.8
Finland	52.3	8.6
Sweden	48.7	9.2
UK	65.5	7.1

Source: Eurostat, 2005.

4) What rate?

With consumption amounting to around 60 % of GDP, on average for the enlarged EU, a flat rate of around 1.5-2% throughout the Union should be sufficient to finance a EU budget of about the present size (1.0-1.2% of GDP). The receipts for all purchases subject to VAT would show the amount paid to the European Union, thus making citizens aware of their contribution. The VAT receipts pertaining to the Union would be transferred automatically and continuously to Union accounts, as they accrue to VAT offices in the member states, and would no longer be shown on national budgets. National budgets would not really be affected, since government could lower taxes (for example VAT) and the lower receipts would be offset by lower payments to the EU budget under the GNI resource.

Under this proposal, ideally the EU budget would be covered by only one tax apart from the traditional own resources), with clear benefits of transparency and visibility. However, Art. 268 requires the budget of the Union always to be 'in balance'. Therefore, some mechanism for ex-post adjustment of revenues in light of actual spending, such as the existing GNI resource, has to be maintained. This mechanism, however, should amount to no more than a small shock absorber to make up for unforeseen differences between actual revenues and expenditures, with net excesses and shortfalls of spending shared on the basis of shares in overall GNI.

An EU VAT surcharge would lead to a reasonably even distribution of the burden, and would not necessarily be regressive. Traditionally, the view has been held that poorer countries have higher consumption as a proportion of income, and hence a relatively larger VAT base. However, the data in Table 4 indicate that among the countries with high VAT revenues one finds both rich (Sweden) and poor (Hungary); the same applies to countries with low VAT revenues in proportion to GDP (e.g. Spain, a cohesion country, and Italy, with GDP per capita above the EU average).

Introducing a European VAT surcharge would not immediately eliminate the view taken by governments that the most important aspect of the EU budget is the national 'net balance', because governments would probably consider that the contributions made by their citizens towards the EU budget should just be seen against the benefits their regions and farmers receive. But the amounts contributed to the Union would no longer appear on national budgets, and the EU citizens would have a direct feel of how much they have to pay for common policies.[4]

5) A new tax?

[4] As an aside, one might note that in general it does not matter whether one uses GDP or GNP as the base for the ability of a country to contribute to the EU (and be eligible for Structural Funds) since for most countries the difference between GDP and GNP is minor, less than 1%. The one important exception is Ireland, where GDP is about 20% higher than GNP. This is attributable to the fact that a large proportion of the value added produced in Ireland (measured by GDP) originates in enterprises owned by foreign firms. This is a consequence of the large amount of FDI Ireland has received over the last decades. Some of the new member countries might soon experience a similar phenomenon since they are also receiving a sustained large inflow of FDI.

The populist objection to this proposal that it would constitute a new tax and thus be politically unacceptable is easy to neutralise: member countries can just lower their national VAT rates by exactly the amount of the EU surcharge: for the consumer nothing would change, except that the VAT receipt would have one additional line.
The biggest advantage of moving to this financing mode for the EU would be transparency also at the moment of budget negotiations. It would require only an agreement on one number (the EU VAT surcharge) and not an ever increasing set of special deals with those member countries that feel disadvantaged by the structure of expenditure.

REDISTRIBUTION OR SUPPORT TO ECONOMIC AND SOCIAL DEVELOPMENT? IT IS TIME TO TELL THE TRUTH ABOUT THE EU COHESION POLICY

Marjorie Jouen

Too often since 1999 and Agenda 2000, the cohesion policy has been described as a purely redistributive policy in the framework of budgetary discussions. This conceptual drift is neither totally the result of chance, nor of ignorance.

The development of such a reasoning coincided with the rise of the 'net contribution' approach and a growing hostility to any increase of the EU budget in the net contributors' camp. The situation worsened when the Enlargement package was negotiated by the end of 2002, accrediting to the New Member States the idea that the Structural Funds compensate both the cost of the adoption of the "EU acquis" and the restricted conditions applied to them for the CAP directs aids, and that they represent the bonus of their accession as less rich countries.

A similar thesis inspired the British government's Green Paper "A modern regional policy for the United Kingdom" in March 2003[1] which broadly promised a budgetary status quo to the English regions (i.e. same amount of money) if they would support the government's proposal to suppress the EU cohesion policy from 2007 onwards. As the cohesion policy was only presented as a redistribution of public money between the rich and the poor regions, the UK government explained that it should be more efficient in suppressing the detour via Brussels and organise the solidarity at national level. Incidentally, it was easy to criticize the complexity of the EU funding rules compared with the rather small amount of money engaged, especially for the richer regions (objectives 2 or 3). But, even if the British regions and the practitioners were not taken in by such arguments, the fallacious thesis continued to prosper in the framework of the Financial Perspectives negotiations 2007-2013.

It may not only be due to the collusion between the macro-economists and the budgetary experts, always keen to find any good reason to reduce public spending. A more political explanation has to be considered. Generally speaking, one must not forget that progress towards European integration has been accompanied by the strengthening of regional and local authorities in the name of democratic progress and greater socio-economic efficiency.

During the last 20 years, the regions and cities have unquestionably benefited greatly from the stable legal framework provided by the Single Market and the impetus generated by the EU cohesion policy. The rules attached to the Structural Funds helped to enhance decentralisation and to press for more local and regional autonomy. To some extent, in encouraging exchanges of local best practices and partnership between all levels of elected bodies, they called into question the national administration's capacities, threatened their monopoly in external relations and forced them to adopt a more transparent and democratic management.

Thus, it is time to restore the truth as regards the EU cohesion policy. It is time to make it clear that this is not just an instrument of redistribution but also, and above all, a tool to enhance economic and social development. If quantitative data matter, qualitative data do too. Therefore, what is at stake when discussing of the future of the EU cohesion policy is both the amount of funding but also the governance of the funds. Neglecting this might undermine the overall EU prosperity and competitiveness[2].

The first part of this paper will recall some basic features concerning the content and the aims of this policy. The second will highlight the results achieved so far and the third will present a new concept linked to this combination of economic and political components of the EU cohesion policy – the leverage effect – that would merit being used in the future.

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[1] HM Treasury, *A Modern Regional Policy for the United Kingdom*, Department of Trade and Industry, and Office of the Deputy Prime Minister, March 2003.

[2] Jouen M., *Adaptation of cohesion policy to the enlarged Europe and the Lisbon and Gothenburg objectives*, Study to the European Parliament, Policy department structural and cohesion policie, IP/B/REGI/ST/2004-008, March 2005

1 – The aims and rules of the cohesion policy

Today, the economic and social policy represents the European Union's second budgetary post, i.e. 0.46% Gross National Income. It benefits all the citizens of Europe, via the co-funding of measures to promote human resources. But, the main share of the subsidies (more than 70%) goes to the less-developed regions, 171 millions inhabitants out of a total of 490 millions.

Historical summary

The bases of the European economic and social cohesion policy were set out in 1986 in the European Commission Paper "Making the Single Act a success". They took shape in the 1988 budgetary reform, when the European budgetary post aimed at supporting economic and social development was doubled, with the view to get a double dividend in the framework of an integrated market: on the one hand, the aids should allow the reduction of the tensions harmful to the harmonious development of Europe, and on the other hand, the richest countries' economies should benefit from an increase in demand generated by the European funds given to their neighbours, in particular through public procurements In fact, ten years later, Europe was regarded positively, registering an average annual growth of 3.2% and the creation of 18 millions jobs. It was also possible to estimate that, due to import leakages (24% on average), more developed regions and countries benefited indirectly from EU funds[3]. The French economy, for example, won back 2.2 Bn € a year between 2000 and 2006 through private companies' exports to the less-developed regions.

This policy was pursued and strengthened in 1994, with a further doubling of the structural funds. Thus, the annual budget dedicated to the cohesion policy grew from 5 Bn € per year in 1986 to 15 Bn € a year in 1995 and reached 40 Bn € per year in 2005.

The implementing conditions

Even if the cohesion policy targets the regions lagging behind, it tries also to prevent that the situation of the richer regions facing structural problems (mainly the rural areas in decline or those in the process of industrial restructuring) from deteriorating.

In order to achieve this two-tier objective, several conditions were requested:

- multi-annual funding (initially of a 5 year duration, now 7 years), ensuring the stability of their resources and the ability to develop medium-term programmes for beneficiaries;
- integration of specialised or sectoral funds, making it possible to draw up multi-purpose programmes combining investment in heavy infrastructures, the building of local facilities, support for modernising business, and the accompanying social measures.
- partnership management between the three levels – European, national and regional or local -, concerning both the definition of the main guidelines, the programming (the choice of the type of actions and the fund-matching), the follow-up of the implementation, and the evaluation. With the view to improving the ownership by the civil society at regional level, the non-governmental organisations and the social partners were progressively involved in the follow-up committees.
- the additionnality principle, which aims at preventing the new programmes from replacing the existing ones at the national or the regional level. A strict ex-ante and ex-post control is carried out to check that the national or regional authorities have not taken the opportunity of new funding to disengage themselves. This very principle helps give priority to measures and policies corresponding to a true Community added-value.
- the concentration aims at maximising the impact of the European funding. It consists in targeting the higher leverage-effect investments, the less-advanced regions or groups, and in graduating the level of aids depending on the needs. However, in order to avoid the disaffiliation of the rich regions, small European programmes for horizontal cooperation

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[3] Beutel, J., *The economic impact of objective 1 interventions for the period 2000-2006,* Final Report to the European Commission – DG REGIO, Constanz, 2002

- and networking have been created to tackle common interest issues, such as cross-border cooperation, urban renewal, rural local development, ...
- the evaluation of the results, which permits on-going adjustments of the measures or the subsidies, according to the change in the environment, new priorities, and last but not least the retention of the money in the event of unsatisfactory implementation.

2 - The achievements

The cohesion policy had a major positive impact in both quantitative and qualitative[4] terms:

- Economic convergence, thanks to the catching-up of the less-advanced countries: the Irish example is obviously the most remarkable, as its per capita GDP increased from 64% of the EU average in 1988 to 118% in 2000, because of an exceptional annual growth of 6.5% over more than a decade. The three other countries, Spain, Portugal and Greece, achieved more reasonable records, since between 1988 and 2000, their per capita GDP grew from 67.8% of the EU average to 73.5%. Despite none of these member States receiving more than 3.5% of their national GDP from the EU, the European subsidies are considered to have contributed to an additional rise of 9.9% in the Greek GDP over 10 years, 14% in the Portuguese GDP, 10% in the Irish GDP and 6% in the Spanish GDP.
- The modernisation and improvement in the effectiveness of the public administration: the conditions imposed for allocating the Structural Funds played a crucial role in changing public management in the regions and member States (financial control, programming development, transparency). Technical assistance, exchange of good practices and twinning contributed to institutional building, a better professional level in the civil services and finally better quality of the services delivered to the public (accountability, e-administration, governance). The partnership in the funding and programming management improved local democracy.

However, it revealed several limits:

- the persistence of inequalities: the growth led to a widening within the countries of the gaps between the remote regions and the central or metropolitan regions, and also between areas at a smaller scale, such as in the inner cities. Some areas often combine social, technological and economic handicaps. Poverty is still a concern for 55 million people in Europe.
- Some regions remain outside the overall movement, because of severe problems of governance (South of Italy), and the informal economy cannot be reflected in the official statistics.
- The most populated countries and the less-opened economies tend to catch up more slowly. There is a time-gap in the perception of the positive effects because of the learning process (5 years at least) and the emergence of a certain fatigue after 15 years cannot be excluded. Then it is necessary to regularly up-date the tools and to provide for a way-out in the event of success (phasing-out system).

3 – The leverage effect

In order to contribute to the debate on the future of cohesion policy in an enlarged Europe and its role in the Union's budget, the Committee of the Regions launched a study in 2006 based on 11 case studies, focusing on the underestimated effects of cohesion policy.

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[4] European Commission, *Unity, solidarity, diversity for Europe, its people and its territory*, Second report on the Economic and Social Cohesion, Brussels 2001

European Commission, *A new partenership for cohesion: convergence, competitiveness, cooperation*, Third report on the Economic and Social Cohesion Brussels, 2004

The CoR proposed adopting a broad concept of the leverage effect, which takes account of a range of factors that are important for assessing the impact of the Structural Funds:

- Financial aspects

According to European Commission's estimates[5], every euro spent at EU level by cohesion policy leads to further expenditure in Objective 1 regions, averaging 0.9 euros. If we consider Objective 2 regions, the average additional expenditure generated rises to 3 euros for every euro invested. It means that the Community expenditure helps to achieve better results and to secure the support of the stakeholders more effectively than expenditure at the national and regional levels. This multiplier is a result firstly of the thematic and geographical concentration of the Structural Funds, secondly, of the wide variety of financing instruments available (e.g. the global grant, risk-capital funds, guarantee funds, loan funds and urban development funds), and lastly, of the strengthening of public-private partnerships, because of its stable financing and multi-annual programming.

- Political and strategic aspects of thematic concentration

Cohesion policy has a key role to play in organising regional and national priorities in such a way as to create synergy at the European level. The European investment strategy concerns areas related to the Lisbon and Gothenburg Strategies, namely education, knowledge, innovation and research, environmental protection, social services, lifelong learning and the establishment of European bodies.

This investment not only affects demand; it also has long-term structural effects on the economy, increasing economic growth and making the regions more competitive. Undoubtedly, cohesion policy provides leverage for sustainable growth that respects the environment, preventing its neglect from becoming a factor that limits growth, as well as the quality of life and conservation of natural resources.

The case studies have also shown that the cohesion policy has focused national policy priorities on areas that are important to economic growth, such as innovation, research and active policies to improve employment and social inclusion. This has helped to raise awareness and to broaden the scope of the "innovation" concept, into regional development strategies. Cohesion policy has led to account being taken of political areas that were previously overlooked by national or regional policies. Broadly speaking, the most flexible and market-focused approaches have been the common denominator for the new approaches introduced by cohesion policy.

- Institutional capacity building

It is worth highlighting the progress achieved by the civil services in promoting partnerships, improving institutional capacity for designing and implementing public policies and extending the culture of evaluation, transparency and exchanging good practice. These factors all form part of the system developed in the European Union for cohesion policy, thus helping to improve governance at all levels, because authorities then apply many of these approaches in other sectors. The creation of new bodies, such as the Regional Development Agencies, has also played a key development role in many of the Union's regions. This has also increased Member States' capacity for adopting and effectively implementing Community legislation in a number of areas, such as the environment, the public procurement law in the Member States and the opening up of public markets to all EU companies

- Increasing cohesion in Europe

Firstly, the principle of partnership and the active role played by leaders has encouraged cooperation between public institutions and the different sectors of society which has played a key role in finding solutions to problems. Secondly, cohesion policy has helped to find multi-dimensional solutions to highly complex and diverse problems; it has led to account being taken of this diversity, especially in the Union's peripheral regions, in those lagging furthest behind and

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5 European Commission: COM(2005) 299. Cohesion Policy in Support of Growth and Jobs: Community Strategic Guidelines, 2007-2013, Brussels, 5 July 2005.

in its outermost regions. This cohesive approach has also had a marked effect on other Member State policies (transport, energy, health, education). Finally it has helped to create the appropriate conditions for cooperation between EU regions and local authorities, especially across national borders. In rural and urban areas, it has effectively demonstrated the added value of European policy to citizens, helping to improve public services and the quality of life.

It should be pointed out that this leverage effect and other cohesion policy impacts occur in all types of region and in a great variety of programmes and projects, irrespective of the project's cost. Because it covers the entire EU, cohesion policy provides a suitable continent-wide framework for ensuring balanced economic and social development. Addressing both convergence and competitiveness factors, it creates the essential conditions for pooling experience and exchanging best practice.

In order to maximise the long-term leverage effect of the Structural Funds, account must be taken of a region's general context and its cultural identity. There must therefore also always be a balanced relationship between EU-wide requirements and regional priorities. Attempting to change the culture and mindset of a given society, by promoting innovation, education, the entrepreneurial spirit and creativity, guarantees that the changes potentially generated by the Structural Funds will be lasting.

As regards the 2007-2013 programming period, the leverage effect of EU cohesion policy can be significantly reinforced. The tried and tested principles underpinning cohesion policy have been complemented by a number of measures: the adoption of a more strategic approach for cohesion policy, earmarking and a greater concentration of funds in priority sectors, an improved legal framework for adopting innovative financing schemes, the attachment of due importance to urban development programmes and upgrading territorial cooperation. These changes have confirmed that, when fundamental EU policy shifts occur, cohesion policy can play a central role in giving practical inspiration and support to economic and social change throughout the EU. The Member States should strengthen partnerships at all stages of the governance and management of the Structural Funds, putting into practice effective ways of involving regional and local authorities and civil society throughout the process. There should be a thorough-going partnership with cities on account of their potential as drivers of growth and employment. The European Commission and the Member States should safeguard the experimental and pioneering role often played by the Structural Funds..

The study led the CoR[6] to recommend that the European Commission incorporate the concept of leverage (with its four dimensions) into its forthcoming evaluation of the current state and progress of cohesion policy. It further noted the need to consider particular regional features at all levels in relation to future cohesion policy, given that "strength in diversity" is a key to the success of the leverage effect of cohesion policy.

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[6] Committee of the Regions, *Opinion of the leverage effect of the structural funds* (CoR 118-2006), March 2007

The EU budget and the financing of European public goods
Maxime Lefebvre

1/ All European public goods don't matter in the same way to the European budget.
For example, regulation activities of the European Union don't cost much money, essentially administrative costs. They cost above all competences to the member States, and contribute to produce public goods. The single currency stabilizes the monetary relations between the countries of the Eurozone, and can be seen a contribution to a better regulation of worldwide monetary relations. The regulations in the field of environment allow the EU to promote a safer environment inside and towards the outside world. The European trade policy creates a common European interest in trade matters, and is a factor of further liberalization through agreements with third countries or with other free trade areas.
In a different manner, several policies of the EU cost a huge amount of money and produce public goods.
The common agricultural policy still represents half of the European budget. One could argue that some benefits of the agricultural policy (such as agricultural self-sufficiency, quality of food, preservation of the countryside, etc.) can qualify as "public goods", but the question remains if they should be financed primarily by the European or by national budgets.
The regional policy makes up one third of the EU budget. It contributes to an economical catch up process in poorer member states. It is an expression of solidarity and of cohesion in the EU, through a redistribution of money from rich to poor member states. This doesn't produce directly some "public goods".
The policies for competitiveness ("Lisbon related policies" : transport and energy networks, research) are still unsufficiently funded. They produce a kind of public goods when the money is better spent at European than at national level. For example an industrial program like Galileo could not be realized by a member state alone.
Above all, the European Union is improving the public goods for Europeans in the field of security. When the EU delivers a common policy in migration, accompanied by a common management of frontiers, it is an improvement for the European citizens who enjoy the free movement of persons on the European territory. When the EU is developing its common foreign and security policy, or its defense policy, it brings public goods which cannot be delivered as efficiently at a national scale (for example peace on the Balkans, or in Africa, or in the Middle East, or in the former Soviet Union, etc.). There is a clear added value of Europe in the production of public goods in this field.
Last but not least, one shouldn't underestimate the benefits of a political union of Europe. Where European nations are able to cooperate together and to develop a common sense of values and of solidarity, they can provide public goods (such as peace and security) not only for themselves but also for the outside world. This brings also to the question of the legitimacy of European institutions, and also of the European budget. The issue of a European tax, which would create a direct link between the citizens and the European institutions, is often discussed. This new form of financing could put an end to short view bargains in the negotiations of the EU budget ("le poison du juste retour", like Pr Jacques Le Cacheux says).
2/ The major challenge for the near future is to decide how a better shaping of the EU budget could improve the production of European public goods.
One possibility would be to increase the overall European budget, which is presently limited to 1 % of the global GDP. This would free new resources for competitiveness ("Lisbon related") policies or for security policies (management of borders, fights against illegal migration, peace keeping operations…). But this is not a very realistic way because the most important member states contributing to the European budget don't seem ready to accept a significant increase in European expenditures. By the way, increasing the European budget would imply an equal decreasing in national budgets, which is not an easy task.

A variant of this first option could be to create a separate budget for the Eurozone, as Jacques Delors already proposed. The Eurozone could have its own structural funds for solidarity and competitiveness expenditures, and even its own budget for security and defense. This means the Eurozone would transform into a more integrated political hard core, whereas the enlarged EU could be reduced to a sophisticated free trade area. This will depend on how ambitious member states will be on the future of Europe.

A second option is not an increase of the European budget, but rather a reallocation of expenditures at a globally stabilized level of the overall budget. André Sapir proposed for example in its report of 2003 to renationalize the Common Agricultural policy, and to allocate these new resources to competitiveness and education. Without going so far, one could imagine that the principle of co-financing be introduced in the funding of the Agricultural policy. The new resources available in the EU budget could lead to a raise of expenditures for research, infrastructures, and also for ESDP (common civilian and military structure security, joint armaments programs, joint operations). Military expenditures could partly be spent more efficiently at the European level, avoiding a useless duplication of national armaments programs.

A budgetary integration of the ESDP would improve the European capacity in producing peace and security. It would improve the political integration of Europe, facilitating a common sense of ambition in this field. It would remedy to the deadlock of the "juste retour" (the less money is spent on agriculture and the more on security and defense, the less justified the "british rabate" will be). Such an evolution would be a contribution to a political union of Europe, which again is a major European public good.

Overhauling decision-making
Stefano Micossi

Decision-making procedures play a central role in preserving the present anachronistic structure of the EU budget, and should therefore be changed.

The EC Treaty has explicit provisions for deciding the system of own resources and the yearly budget, but not the MYFP, which is where all the key budgetary decisions are taken.

The system of own resources is decided by the Council by unanimous vote, based on a proposal by the Commission and after consulting the Parliament. The decision thus taken is then recommended for adoption by the member states "in accordance to their constitutional requirements" (Art. 269).

Decisions on the yearly budget are taken by Council (by qualified majority) and Parliament (by absolute majority) together (Art. 272); Council has last say over 'compulsory' expenditures,[1] which notably includes the CAP, and Parliament has last say over the rest of the budget. The budget has to cover all expenses of EU institutions (universality) and must always be in balance. The Commission prepares the preliminary draft budget, but subsequently has no formal role in the decision. Nevertheless, it is responsible for executing the budget.

The system of the MYFP was agreed at the end of the 1980s, after years of bitter contests between Council and Parliament that had led to paralysis and in two instances to rejection of the budget by Parliament (in 1979 and 1984). Under this new system, the Council fixes by unanimity the MYFP for a period between five and seven years, which include annual ceilings for total resources and the main headings of spending. The initial proposal is prepared by the Commission, but the Council may modify it as it wishes. The European Parliament negotiates with the Council and then votes a resolution, by simple majority, accepting the Council decision. In practice, it has had little influence on the main figures – for the CAP and structural spending – but has used the opportunity to extract concessions concerning its own interests, e.g. the influence of the EP in other areas.

The MYFP are then enshrined in an inter-institutional agreement that binds Council, Commission and Parliament to 'loyal cooperation' in yearly budgetary decisions, and notably to respect yearly expenditure ceilings.

It should be noted that these arrangements are not codified in any legal document setting out budgetary procedures, but are renewed by consensus by the three institutions at the expiration of each MYFP.

There are three main drawbacks in this system. First, the yearly budget – which is the instrument with legal value under the Treaty – is not the real seat of budgetary decisions, which are taken elsewhere. Second, all significant decisions are in practice taken by the Council, outside the Community method and based on intergovernmental negotiations where every member state has veto power. Third, the MYFP are adopted for time periods that are completely disconnected with the time interval of legislatures and Commission tenure.

The Constitutional Treaty would have improved this situation considerably, but more could be done. The MYFP have been brought into the Treaty[2] and will take the form of a European law of the Council, still decided by unanimity, after obtaining the consent of the European Parliament; the Commission has no formal role of proposal. Furthermore, the category of compulsory

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1 Compulsory expenditures are only obliquely referred to in Art. 272, paragraph 9, of the EC Treaty: "A maximum rate of increase … shall be fixed annually for the total expenditure other than that *necessarily resulting from this Treaty or from acts adopted in accordance therewith*". The precise classification of expenditures falling within this category can be found in annexes to the inter-institutional agreements.

2 Articles III-402-415.

expenditures has been suppressed, thus broadening the Parliament's vetting to include the entire yearly budget.

Clearly, the Union will not have a proper budget, as an expression of its priorities and policy goals, until both the MYFP and the yearly budget are decided by co-decision of Council – deciding by qualified majority vote – and Parliament, perhaps based on a Commission recommendation, but not a legally binding proposal – since this would represent an undesirable limitation of Council and Parliament's freedom to act on the common budget. However, this decision-making power should not extend to the decision on the total resources ceiling, since the latter impinges on national parliaments' taxation powers. Moreover, the European Parliament is likely to have a bias in favour of more spending at the European level.

As we have argued, there are a number of areas where the greater European interest might best be served not by more spending at the EU level, but by other measures, for example increasing competition or coordination of national policies. A counterweight is thus needed to limit overall spending.

One way to do this would be to leave the last word on total resources to the Council, but let the European Parliament determine their allocation across categories of spending. Such a distribution of competences is likely to lead to a useful implicit negotiation in which the allocation of spending proposed by the European Parliament would be accepted by the Council to the extent that it reflected European interests and 'value for money'. Were this not the case, the Council would reject the demands for a higher resource ceiling, and cut it to size.

Another beneficial change, which does not require a change in the Treaty, would be to synchronise the reference period for the MYFP with the terms of office of the Parliament, so as to strengthen the interrelation between budgetary decisions and the results of the European elections. The MYFP should run for five years, and enter into force one year after the election of a new Parliament, to allow it sufficient time to deliberate after election.

With this change, the content of the MYFP would become a main theme in the campaigns for the election of the European Parliament, with a likely increase in voters' interest in the elections and their turn out.

The European Parliament could send out the right political signals, once it starts its own work on the new MYFP. It should tell the Council that it will accept whatever ceiling member states put on overall spending, but at the same time that it will expect to have a main say over the composition of spending, and it should indicate what expenditures it considers a priority.

In this game of self-restraint, the Parliament, by accepting the ceiling on total expenditures, will gain credibility with governments and the electorate. In exchange for this, it will affirm its role in deciding what European public goods should come from the Union budget.

Reforming the Own Resources System: What for?

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Paper prepared for the seminar "The EU budget: What For" in Brussels, 19 April at the Committee of the Regions

Abstract

This paper concentrates on the present debate revolving about the need to create fiscal own resources or introduce automatic correction mechanisms. It questions the capacity of these options to solve the problems of the EU budget and in particular the net balance disputes. The basic structure of the own resources has a number of positive features that should not be traded for questionable benefits. The paper also presents three different reforms for the own resources, which even if politically provocative present the own resources dilemma from a very different angle. Finally, real problems lie elsewhere, and issues about reforming expenditures and the decision-making procedures are addressed.

1. WHAT ARE WE TRYING TO SOLVE BY REFORMING THE OWN RESOURCES?

The Own Resources of the European Union face many criticisms. The most repeated accusations are that it is not a fair system, that it is opaque and that it is not really an own resource, because it largely constitutes of a direct transfer from the member states. The lack of real EU owned resources is pinpointed as the reason for the concentration of member states on their net balances. The UK rebate being one consequence of having resources based on member states' contributions.

This is, however, an oversimplification, the own resources are a victim of disagreements on expenditures. While net balances always play some role, these become a central issue when member states consider unjustifiable to use their taxpayers money for policies which are not defendable domestically. Solidarity from member states can only be requested for policies which are clearly benefiting a common accepted cause.

Given the inability of the EU member states to agree on an acceptable expenditure structure, own resources are used to "compensate" those member states that feel unfairly treated by the *expenditures*. Most member states agree that policies should be revisited. Academics, politicians and civil society representatives generally agree that the budget is not addressing present EU priorities and they wonder if it the present policies are actually effective and their size justifiable. Reports of EU money being misallocated require politicians to act in front of the electorate accordingly. Thus, net balance disputes and ensuing distortions on the resources side have an important link to policy quality and not only to financial returns.

Solidarity from member states can only be requested for policies which are clearly benefiting a common accepted cause. It is short-sighted to believe that member states' behaviour is dictated solely by balances in total independence of the policy mix, but these will certainly behave so when they do not consider the expenditures acceptable.[1] The game thus becomes a pure accountancy exercise where transfers back are maximised and contributions minimised, regardless of the resource source. The result is then dictated solely by member states' voting power in the terms described by Widgren (2006)[2]. Under these conditions and regardless of the resources system, net balances would always stay similar whatever the resource system.

As long as there are strong disagreements on the quality of the expenditures it is unlikely that any resource system would eliminate the net balance considerations. One has to only look at federal states to see that contributions based on tax sources do not eliminate at all issues on financial redistribution at national level. In the EU, where arguments for redistribution are more difficult to defend, it is unlikely that net balance considerations would be reduced.

While this paper argues that Own Resources reforms should not be undertaken in order to solve net balance problems disappear, it does claim that reforms could have some impacts by changing the incentives of member states to stick with the present policies. These reforms, however, are not the ones usually discussed. These are not tax based, taxes being reserved to a time when the expenditure priorities are more coherent and the decision-making procedures on EU policies have been reformed.

2. QUALITIES AND WEAKNESSES OF THE PRESENT OWN RESOURCES TO PRESERVE

Despite many misgivings, the current system has certain crucial advantages, which makes it difficult to find comparable alternatives: simplicity and cost effectiveness (of the basic system before rebates and concessions), long term stability and predictability, a guarantee of budgetary balance and a distribution of the burden between Member States closely proportional to GNI.

Additionally, from the point of view of fairness of contributions, the present sources of financing, (Traditional Own Resources (TOR), virtually harmonised TVA and GNI contributions) score well. These contributions are closely related to the contributory capacity of member states expressed in national income. The UK rebate and other concessions to individual members, affect this relationship disrupting the fairness of contributions. However, the origin of these corrections is to be found in the distributional implications of expenditure policies. Member states do not openly challenge the notion of contributions based on the share of GNI, but rather those deviating from it. It is difficult to find strong real weaknesses to the basic system of own resources.

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[1] That policy acceptability and distributional issues are important is demonstrated by the UK rebate. It is not very surprising that the UK, which in 1984 was one of the poorest member states, would not consider justifiable to finance an agricultural policy which benefited more other wealthier members. On the other hand, it is also not surprising that nowadays main contributors to the EU budget would seek to reduce their contribution to finance the rebate. The UK has become one of the wealthiest member states of the EU and it still considers unjustifiable to finance the Common Agricultural Policy because it disagrees with the policy's structure and aims.

[2] Widgren (2006), 'Budget Allocation in an Expanding EU', SIEPS, Sweden.

3. INTRODUCING CORRECTION MECHANISMS OR TAXES?

Given the points raised above, one could conclude that there is no point in reforming the Own Resources. This is not the case, but the real underlying causes for the problems on the expenditure side have to be taken into account before launching politically correct and theoretically attractive reforms which then fail to work under the real conditions. There is a risk of delusory solutions in both, the introduction of a generalised correction mechanism and the introduction of tax based resources.

3.1. The generalised Correction mechanism

The European Commission is aware of the impossibility of introducing quickly a tax based system in the shorter run and proposed a generalised correction mechanism in the 2004 report on own resources, which should in fact be a system based on the present political reality. This system did not attract much interest and is in fact neither a solution, nor a good system to promote reforms on the expenditure side.

This mechanism is a complex system designed to grant automatic rebates to member states whose net contributions exceed a certain percentage of national GNI. While the mechanism undoubtedly has some merits, it does not offer any particular benefit to the net contributors above the present system. It also does not address the concerns on the origin of the problems, i.e. the expenditure policies. The UK would, for example, lose a large part of the rebate while not gaining any change on the expenditure side. In addition, *it also would introduce rebates as an automatic response to net contributions regardless of the merits of the policies financed*. Should member states be allowed to obtain a rebate *automatically* on policies which are the result of a consensus agreement? One should also add that there is *no guarantee that the results generated by a generalised mechanism would please net contributors and would avoid additional ad hoc measures* for specific countries.

3.2. Tax based resources

It is often argued that the introduction of resources based on owned fiscal means, i.e. EU taxes, would eliminate the net balance disputes and also increase the visibility of the EU budget to the citizens. Both arguments are attractive, but stand on a very unrealistic perception of reality.

Net balance disputes do have an important link to policy quality and not only to financial returns. The lack of common ground on the value of certain main budgetary expenditures has increasingly placed net balances as a central budgetary argument.

Under this conditions, would a change to fiscal own resources matter much? Probably not. The main additional benefit of other sources based on fiscal measures would be the independence of the tax from the national budgets. However, given the easiness in which member states can verify the geographical origin of the tax collection point (national tax authorities would still collect it), these will most likely be treated as a national contribution in practice. This is easy to envisage, as net balance disputes can be found in many federal states. In a structure like the European Union, with veto powers on resources for each individual member state, corrections for an “excessive” tax burden would soon be requested. Corrections which could be much more complex than the present ones, due to the likely further deviation of contributions to national income.

On visibility, the argument also stands on thin ground. Yes, the EU budget is opaque and has little visibility, but this is relative. Citizens generally are not very well informed about their contribution to national expenditures through taxes either, making their contribution visible to policies equivalent to 1% of the EU's GDP seems rather irrelevant. Visibility can also be achieved by allowing member states to identify *nationally* an EU component in a national tax (i.e. 2% of VAT, x% of income tax, etc.), whose yearly aggregate represents roughly the value of the transfer to the EU. Member states need not even use a share of the same taxes.

This would actually better represent the actual cost to citizens, as a visible EU tax (e.g. real VAT) that would only cover part of the budget (which would be the case for fiscal resources as proposed by the Commission), would not reflect the value of the contribution, misinforming the citizen by making only half of the contribution visible is not the objective.

Furthermore, is the EU budget so invisible? Its size is constantly publicised, probably more than the size of any national budget. Net contributors make quite clear to the public how much they are contributing to the budget. Citizens are, however, rather uninformed about the relative size of the EU budget compared to national expenditures, but this is mainly because citizens are not well informed about the size of their national budgets.

Furthermore, making the costs visible but not the benefits is a considerable problem. What is the value added for the citizen for their contribution? The global benefits of membership of the EU and the positive value added of the policies financed by the EU budget have to be clear. Unless EU policies and their importance become much better documented and expenditure policies more related to the needs of the EU and its citizens, visibility of the costs alone makes little sense, unless we are trying to encourage citizens' misapprehensions on the EU.

4. WHAT TO REFORM FIRST? THE CHICKEN OR THE EGG?

Reforms on the expenditures seems to be a precondition to allow a fundamental reform of the own resources. Furthermore, presently, a real reform in expenditures has to be followed *immediately* by a reform in the resources system. If a fundamental reform of expenditures is finally achieved, the rebates and other manipulations on the resources side have to be abolished in the name of fairness. The link between the two is not automatic though.

It would be interesting to adapt the Own Resources first, so as to partially eliminate perverse incentives to keep the expenditure status quo, or to incite reform in the shorter run. Some provocative options are presented here, which brake away from the traditional systems proposed. Regardless of their feasibility, they do allow an alternative vision of the budget and its resources. These are a "reverse correction mechanism" imposing minimum net contributory levels to wealthy member states, a separate resource for the CAP and a more traditional idea of compensation through a special "off-budget" correction heading.

4.1. The 'reverse' correction mechanism

Some member states endorsed the idea of the Sapir report[3] to exclude wealthy member states as beneficiaries of the EU budget. These member states should according to the report be able to finance the policies from their own pockets. Such an option while theoretically more efficient could have quite strong perverse political implications which need careful consideration. EU policies should be for EU citizens regardless were they are located as long as they fulfil the eligibility criteria. If the distribution is under cause, then the eligibility criteria need revision.

It is certainly odd, however, that some wealthy member states are such small net contributors. Studies show clearly that especially due to the CAP, a regressive distributional policy, EU budget distribution is not in line with cohesion objectives and is practically unrelated to GDP per capita (despite the fact that most of the budget is considered presently linked to cohesion). This oddity ensures that some wealthy member states are low net contributors or even net beneficiaries. Of 27 countries in 2013, only 9 are expected to be net contributors and 3 will be considerably important net contributors without a clear any relation to their relative GDP.

It is thus interesting to consider the impact of a "reverse" generalised correction mechanism, where wealthier countries are imposed a net contributory floor, eliminating low and negative net contributors for those countries with a GDP per capita above the EU average. By the estimations of the author, if every country with a GDP per capita above the EU average financed a minimum of 0.35% of their GNI in 2013, this would reduce the contributions of other member states by 8 billion €[4]. The redistribution of expenditures would reduce the contributions of other member states by 0.1% of GNI. *For the UK this system would have a nearly equivalent impact on its contributions as with the system agreed in for the next FP in 2013. It would also eliminate from the net contributors any net balance consideration when deciding on the CAP.* While such a system is unlikely to exist, the political implications are excellent food for thought.

4.2. Separate resource for the CAP

The CAP's perverse allocation is often presented as the cause for the UK rebate. Is the UK rebate justified given the distribution of the funds? Table 1 presents a calculation of the net contribution of the member states to the CAP in 2003. 2003 figures are used to avoid the problems of transition payments in the new member states. The logic works with any number of countries and having 27 would not add to clarity. This has been calculated assuming the CAP is financed by the GNI resource, thus each member state contributes to the policy based on its contributory capacity in terms of GNI. Under this

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[3] Sapir A. (2004), 'An Agenda for a Growing Europe: The Sapir Report', Oxford University Press.

[4] Own calculations, administrative expenditure has not been included to avoid penalising Belgium and Luxembourg for housing the EU institutions

assumption, then the UK in 2003 (without the rebate) would have contributed 7,8 billion € or 17,7% of the CAP and the largest share as percentage of GNI. France paid a similar amount 7,6 billion €, but received over 10 billion € for its farms, a net benefit of just under 3 billion €, despite that neither farm incomes nor national income would warrant such a difference. Interestingly, the UK rebate ensured some fairness in net contributions, by forcing France to become a net contributor, otherwise in 2003 the country would have had a net contribution of nearly 0% of GNI. However, it is unclear why all other countries should pay for a Franco-British equilibrium.

Table 3. Share of contributions to the CAP and net contribution to the policy (year 2003)

	Estimated contribution to the CAP	Share of contributions	Receipts from the CAP	Share of receipts from the CAP	Net contribution m €	Net contribution as GNI % to the CAP
Belgium	1271	2.86%	1025	2.31%	-246	-0.09
Denmark	858	1.93%	1224	2.76%	366	0.19
Germany	10159	22.89%	5877	13.24%	-4282	-0.20
Greece	720	1.62%	2762	6.22%	2042	1.24
Spain	3478	7.84%	6485	14.61%	3007	0.38
France	7626	17.18%	10464	23.58%	2838	0.18
Ireland	524	1.18%	1965	4.43%	1441	1.24
Italy	6027	13.58%	5393	12.15%	-634	-0.05
Luxembourg	12	0.03%	44	0.10%	32	0.15
Netherlands	2117	4.77%	1397	3.15%	-720	-0.16
Austria	1052	2.37%	1128	2.54%	76	0.03
Portugal	622	1.40%	856	1.93%	234	0.18
Finland	684	1.54%	876	1.97%	192	0.13
Sweden	1374	3.10%	867	1.95%	-508	-0.18
UK	7854	17.70%	4014	9.04%	-3840	**-0.22**
Total	44378		44378			

Source : Commission (2005) and Own calculations

The CAP is a redistribution policy based largely on share of agricultural land and historical production. It contributes to the economic strength of the sector and it is unclear that taxpayers in one country should be contributing to it in relation to higher historical yields in another member state. Why should in fact a Portuguese, British or German taxpayer support the successful producers in France, Denmark or Ireland?

This calls either for a radical reform of the policy and distribution of the CAP or for a new method of financing the policy which relates more closely to the sector and corrects for the perverse incentives created by the combination of contributions based on GNI and support based on historical yields.

If redistribution of the CAP expenditures among member states is not justified, then member states could finance the CAP in proportion to the benefit they derive from the policy. The Table below describes a system in which the contribution is based on the GVA of the agricultural sector (and more precisely, the supported products) in the member states. Why GVA? The GVA of the supported products reflects the benefits of the policy better. If for example a country has a low GVA in agriculture for the products it produces, then it will contribute less towards the policy and vice-versa. With this method, while not making the farmer pay the policy, the distribution of funds can be viewed as a cross subsidisation within the sector.

For the UK, while its share of GVA is estimated at 8,64% of EU production, it pays 17,7% of the agricultural budget. Similarly, Germany pays 22,89% while its GVA share is only 13,24%. France pays a similar amount as the UK, 7,6 billion €, but with a GVA in the supported products of 22% of the EU, it received 2 billion € more for its farms than it paid. From this point of view, the budget appears to support clearly the sector of countries where it is already the strongest, rather than the reverse. The lose relationship between the wealth of member states and the net contribution to the CAP as share of GNI is striking. Luxembourg is often appearing as a net recipient due to the presence of the EU administration, but that it is a net recipient of the CAP it is an issue to reflect on. Similarly, Ireland, being the richest EU country also benefits handsomely, as do Denmark or France.

Renationalising the direct payments of the CAP has often been presented as an option, but this does not improve the policy. It reduces the EU budget size, but the reduction is virtual, as expenditure on the Common policy would not change in size. The change is in many senses cosmetical. However, renationalisation is also considered as a system to link the beneficiary countries more directly to the cost of the policy on their territory, counterbalancing part of the regressiveness of the policy. Rather than renationalising the CAP, it is possible to finance the CAP in line with the GVA of the supported products (Table 2).

In a GVA based system, the weight of the support for specific products and the value of production are the main variables. The elegance of this method is that it allows linking the support to the structure of the sector in each country. Ireland is still a large net beneficiary of the policy, for example, due to the diary and beef sectors. Spain on the other side would be a net contributor. The issues now are not any longer the overall net balance, but the distribution of the support between agricultural products! The cross-subsidisation in the sector is laid open and not blurred by the GNI distribution of the financial burden, changing the dynamics of negotiations.

The UK rebate would also become obsolete. According to this calculation the UK would have been contributing 4 billion € and Germany 6.6 billion € less to the budget in 2003 under a budget without rebates.

Table 2. Share of contributions to the CAP in relation to share of GVA (year 2003)

	Receipts from the CAP	est. share of GVA of EU agriculture	Payments based on GVA of agriculture	net contribution to CAP	Net CAP contribution as GNI % to the CAP	Change in net CAP contribution as % of GNI	Change in net CAP contribution compared to previous system
Belgium	1025	2.41%	1068	-43	-0.02	-0.07	-203
Denmark	1224	2.74%	1214	10	0.01	0.18	356
Germany	5877	13.89%	6166	-289	-0.01	-0.18	-3993
Greece	2762	4.49%	1991	771	0.47	0.77	1271
Spain	6485	15.53%	6894	-409	-0.05	0.44	3416
France	10464	21.99%	9759	705	0.04	0.13	2133
Ireland	1965	2.19%	971	994	0.86	0.39	447
Italy	5393	15.97%	7089	-1696	-0.13	0.08	1062
Luxembourg	44	0.11%	49	-5	-0.02	0.17	37
Netherlands	1397	4.92%	2185	-788	-0.17	0.01	68
Austria	1128	1.97%	874	254	0.11	-0.08	-178
Portugal	856	2.30%	1020	-164	-0.12	0.30	398
Finland	876	1.31%	583	293	0.20	-0.07	-101
Sweden	867	1.53%	680	187	0.07	-0.25	-694
UK	4014	8.64%	3836	178	0.01	-0.23	-4018
Total	44378		44378				

Source: Own calculations

4.3. Expenditure side corrections

Proposals to just grant rebates through the expenditure side have usually been dismissed. Apart from the obvious bad image of such transparent transfers, one of the main arguments against these is that it would increase the size of the budget, while obscuring the real contribution of member states. This does not need to be so, it would make the rebates or ‘reimbursements’ clear, making transparent the opaque reductions through rebates and TOR, VAT or GNI alterations. The basic Own Resources could then be based on common rules for all, as rebates would be undertaken through transfers from the budget. This would not necessarily breach the budget ceiling, if such transfers are not accounted as part of EU budget expenditures for its calculation.

5. REFORMING DECISION-MAKING

Most problems on the side of own resources are symptoms of problems at the expenditure side, and those expenditures are based on the result of negotiations ruled by decision-making procedures. If there is a fundamental dysfunction it has to be ultimately the result of the decisions made, and if there seems to be a blockage to remove them, then the present decision-making process has to be inefficient for the task. Of course, decision-making processes in a multinational system tend to be unanimity based, or at least near to requiring unanimity. This can be a real problem for a single market with quasi federal powers in certain areas. Policies that are benefiting the EU as a whole will often not benefit in the same way all countries and the more there are, the more difficult is it is to introduce any policy, especially if it entails financial transfers. Policies supporting a heterogeneous productive sector are the worst served by such a decision-making system, and such is the case for the CAP. Balancing the benefits for all member states requires inventing relationships that do not exist, such as linking the expenditure distribution and own resources, or CAP payments and structural payments (the invention of the Objective 6).

The main power of decision-making rests in the Council, and decision-making is in all areas close to unanimity, before and after the introduction of constitution type reforms. In fact qualified majority voting is very close to a unanimity requirement and the double majority of votes and population only reinforces it. 75% of votes in the council does not translate into 25% of chances of approval of a policy (random voting), as countries vote in blocks of votes, reducing the chances to less than 5%. The council resembles a parliament with 27 parties and very loose governing coalitions in constant instability. To this we need to add the weakness of a European identity and interest, a national interest can ultimately unite national parliamentarians.

For policies of European interest, and specially policies financed by the EU budget, there is a need to shift the decision-making procedure to a more pan-European body, and that is the European Parliament (EP), which by virtue of the transeuropean party groups can take less nationally centred decisions. The anonymity of voting also allows parliamentarians to vote on EU policies without having to defend a national interest in the way a national government is compelled to in the Council.

In the short term, a fast shift of power to the Parliament is not to be envisaged. However, for the EU budget the parliament should take the responsibility for the resources levied. It should be possible to envisage a situation where the EP as directly elected representative of the EU citizens has to approve Commission proposals for policies and budgetary resources *before* the Council deliberates on them. This reversal of the process puts the EP as clear co-owner of policy proposals and also responsible for the quality *and cost* to the citizens of those.

6. CONCLUSIONS

The current own resources system has certain advantages which should be seriously considered before introducing any change, i.e. simplicity and cost effectiveness, long term stability and predictability, a guarantee of budgetary balance and a distribution of the burden between Member States closely proportional to GNI. Changes in the Own Resources should be undertaken with extreme care to avoid trading off these qualities without obvious advantages that work in practice.

Furthermore, the main problems of own resources have their origin in the expenditure side. As long as member states do not agree on the policies and their distributional effects, any own resource system, tax based or not, will suffer from “corrections”. There is no resource system that will silence the complaints of net contributors as long as there are disputes on the objectives and impact of the expenditure policies. Under a tax based system there is even a risk of a wider number of corrections, as countries feeling unfairly affected by the taxes may request compensation in one form or another. These compensations would not necessarily be restricted to excessive net contributors.

Similarly, a generalised correction mechanism would unlikely be stable, as it assumes that member states would be content with the system. It is also questionable if the EU should institutionalise any automatic system granting rebates for policies agreed by consensus, rebates should stay an oddity, not an institutionalised reality.

There are other options to handle disputes over the Own Resources. Three are presented in this paper:

First and foremost, if countries have reasonable grounds to consider their net contribution excessive a correction could be agreed openly through the *expenditure side*. This expenditure can be excluded for the purpose of setting the ceiling of the EU budget expenditures, as it is a de-facto rebate.

Second, the small net contributions of some wealthier member states, and even net receipts for some, call into question the question of solidarity. This paper has presented a *reverse correction mechanism*, which ensures that net contributions of wealthier member states reach a minimum net balance. The implications are interesting.

Finally, if the CAP is considered a root for the present problems in the resources, it is possible to consider an alternative financing mechanism for the policy. The *CAP could be financed separately, with a contribution reflecting the agricultural sector's economic strength*, rather than national wealth. Ultimately, policy decisions would have an element of transfers within the sector.

For fiscal resources, if introduced, should be chosen with extreme care. These are also to be avoided before fundamental reforms in expenditures. Taxes may in theory have many advantages from the point of view of accountability and transparency, but the practical difficulties, operational and political, are often underestimated. For longer term stability, before any important fiscal resources are introduced, the decision-making procedures should also be improved.

The EU budget and stabilisation
Jean Pisani-Ferry (Bruegel)

Starting points :
- Does stabilisation matter ? I will assume it does
- Does it need to be improve in the EU? I will assume it does

Does it follow that there is a stabilisation role for the EU budget?
Three basic reasons for doubt
- Too small
- Spending is rigid
- The EU Budget is for the 27, 14 of which have independent monetary (and fiscal) policies. Even taking into account currency boards, important countries remain out.
- Assuming those difficulties can be overcome, why should we have n + 2 instruments for stabilisation? Would involve considerable complexity

One step further: Let me play the devil's advocate and discuss when and why we could need the EU budget to enter the stabilisation game
This could be:
- Because FP would have to support, or substitute, monetary policy, and in addition
- Because national FP would not be able to do the job

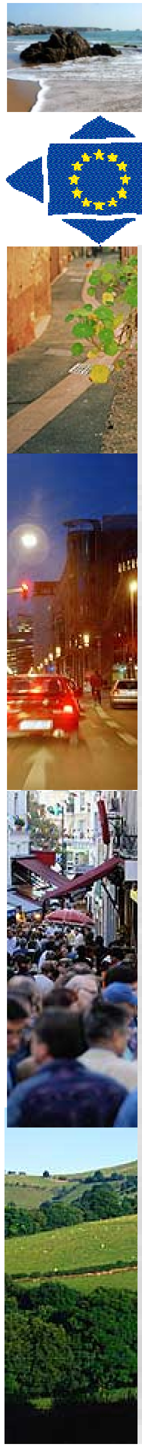
a) When can fiscal stabilisation be needed at the aggregate level?
- Because of a need to support monetary policy in when economic conditions imply limits to interest rates tightening (e.g. financial fragility, already appreciated exchange rate)
- Because of a need to substitute MP when it has become ineffective. Classic example is the liquidity trap
- (There could also be an intention to counter MP but this cese can be excluded as MP would win)

b) Why would national policies be unable to do the job?
- Most of the time they would. There are coordination problem but they can be solved (either through ad-hoc coordination or institutionalised devices, such as rainy-day funds..)
- Exception is when national fiscal policies are paralysed because they are geared towards consolidation while stabilisation calls for expansion

Summing up, we would need MP to be in a in a mess, national FP in a mess too. Would the EU budget save us? No (the impulse would need to be bigger than feasible for the EU budget). Why should we plan for that?

Nevertheless the idea comes up and up again. Why? What is its attraction to some people?
- Illusion that there is potential for debt creation to tap. But:
  - There are no alternative taxpayers. They are the same.
  - As long as EU budget is financed by contributions, the EU and national budget are subject to the same inter-temporal budget constraint (the more MS are indebted, the less the EU can be)
- Way to make room for permanent increase in EU budget
  - Is it a desirable strategy?

A separate issue
- This does not mean the EU budget must be balanced. There can be other reasons to change the way the EU budget is managed (e.g. allow more inter-temporal smoothing)



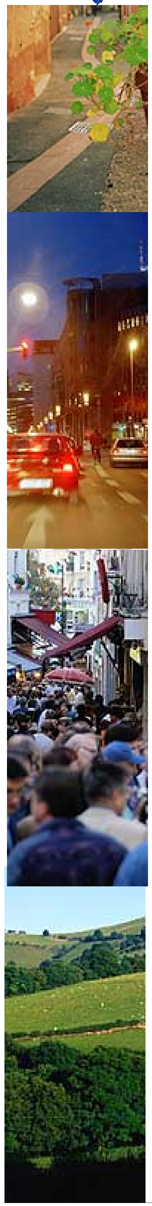
EU budget, redistribution and cohesion policy

The EU Budget: What for?
Brussels, 19 April 2007

Gianluca Spinaci
Committee of the Regions

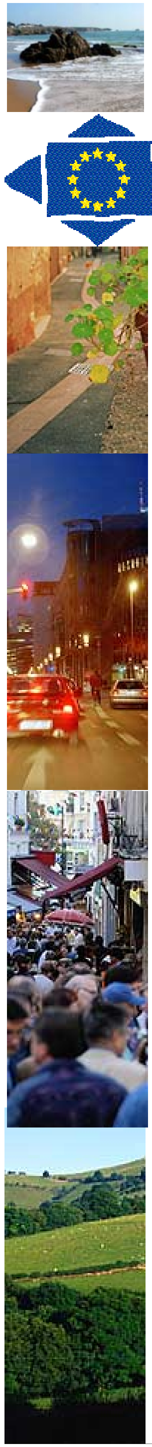
Lisbon: a competitive and cohesive Europe!

Where to invest?
Who does pay for?



Do we need redistribution policy within EU budget? Probably yes

Is redistribution only a financial issue? Probably not



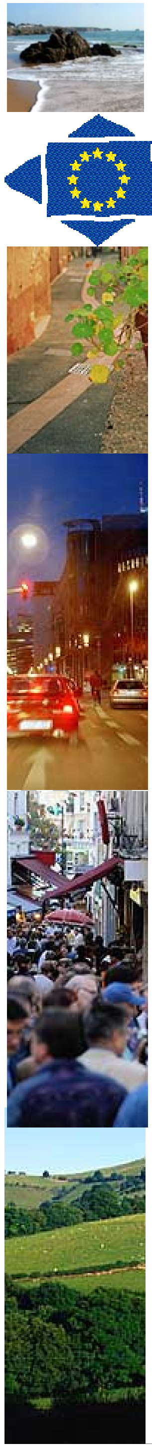
Let’s take cohesion policy

It is a community policy
for cohesive development and grassroots innovation
with redistributive effects:

- Between rich and poor (funding) but also...
- between territories (development opportunities)
- between policy priorities (strategic allocation, earmarking)
- between knowledge level (experience exchange)
- along the time (long-term investment)
- across the institutional set-up (multilevel governance)

- Last but not least, its co-funded investments generate a *retour* effect, with substantial benefits for net-payers

Redistribution does not work as one-time switch of money, but rather as a more complex, dynamic and interactive process with spill-over effects and triggering mechanisms



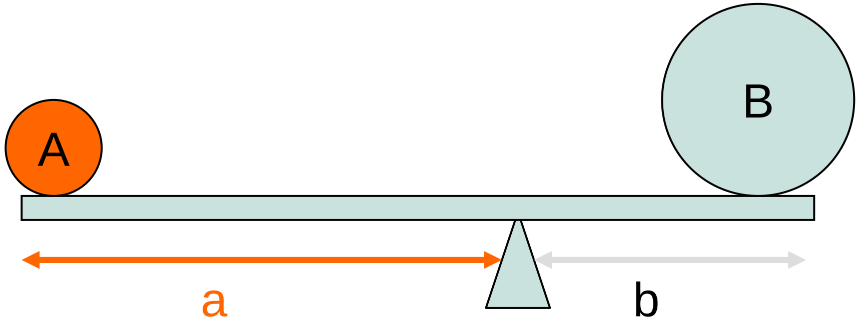
CoR Outlook Opinion

Leverage effect of Cohesion Policy under Structural Funds

based on case-studies

and research report

Leverage principle:
from inertia in physics...

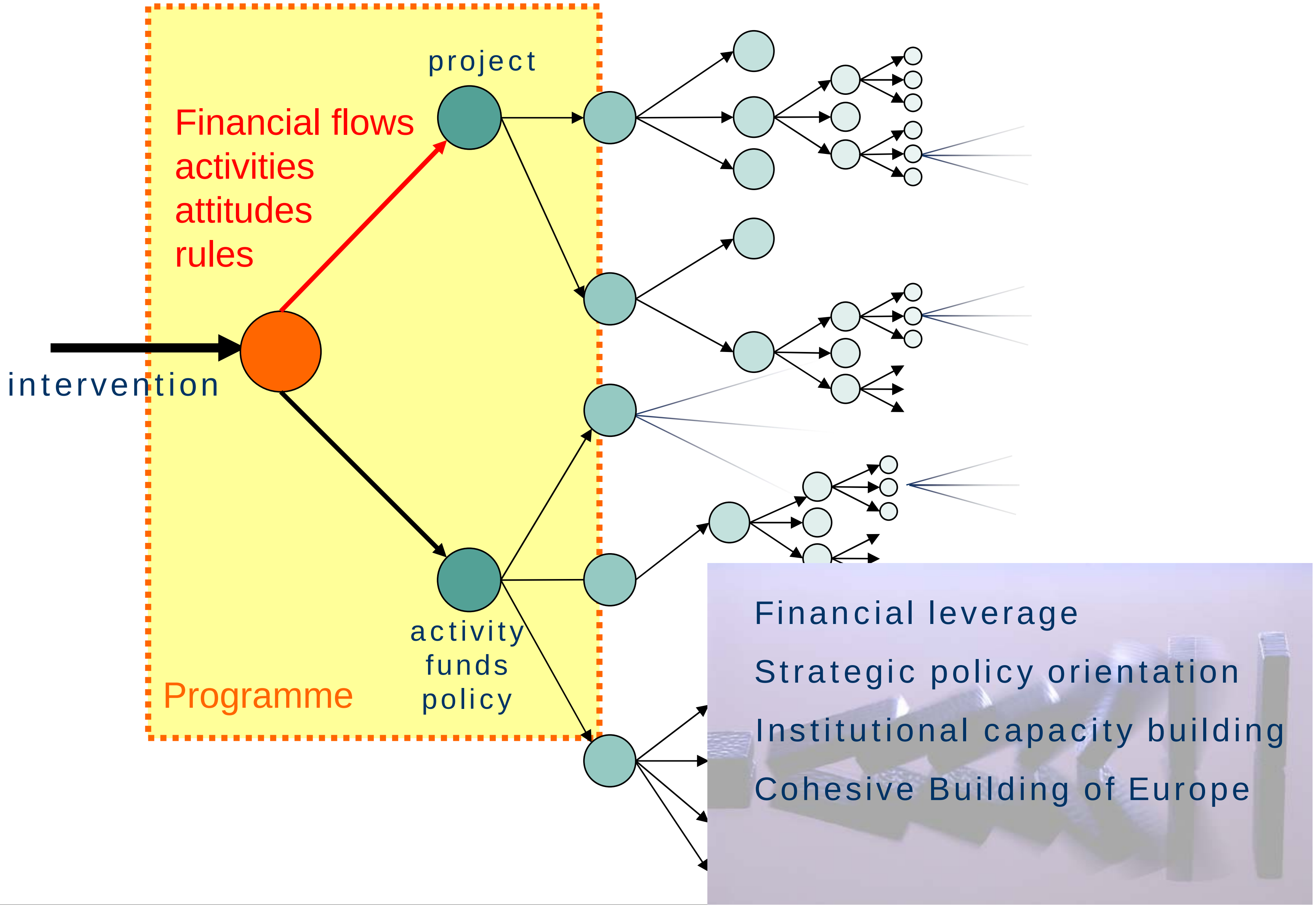


$A \times a = B \times b$

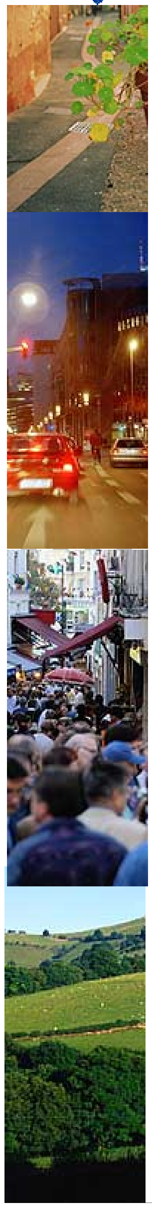
Archimedes described leverage in 300 BC, as a ...

means for converting a small force into a larger one
➔ move heavy obstacles

… dynamics in Cohesion Policies



The financial leverage effect



one Euro, invested at EU level (ERDF) for cohesion policy, generates

Additional investment of 1 Euro in those regions under Objective 1

Additional investment of 3 Euro in those regions under Objective 2

(European Commission)

The financial leverage effect

- Concentration ➔ critical mass
  - Larger investment project
  - Thematic/geographical concentration

- Attract other financial sources
  - levers wide range of funds (local, regional, national, ESF, ERDF, LEADER etc)
  - EIB ➔ private funds
  - guarantee bank involvement ➔ other sources available, too
  - Counter guarantees by EIB allows better terms for SME

- Involvement of the private sector
  - Global grants
  - Financial products with regional banks

Strategic policy orientation

- **Introduction of new policy approaches**
  - Orientation on innovation and development ,
  - Awareness on sustainable development (environment and quality of life viewed as positive factors)

- **Reinforcing EU policy priorities in national policies – flexible and market oriented approach**
  - Active labour market policies
  - Social inclusion
  - Cross boarder services

Institutional capacity building

- Input and output of implementation

- Manifold types and shapes of new capacities
  - Specific team structures
  - Flexible and efficient management structures supported by external expertise
  - Setting up multidisciplinary teams
  - Improving skill level in financial engineering
  - Implementation of competitive calls
  - New projects financing methods,
  - Dealing with external tools,
  - Combination of grants and loans
  - Strategic local partnerships

Institutional capacity building

- **Principles of SF shape policies, institutions and themes**
  - Improve cooperation between stakeholders
  - Greater autonomy to local level, strengthen bottom up approaches, endow local level with project development capacities
  - Improvement in legislation on public works
  - Application of transparent procedures (like evaluation of applicants, communication with intermediaries, reporting)

Cohesive building of Europe

- Active participation of various groups in policy formulation and implementation

  - Inclusion of a variety of stakeholders – agriculture, SME, local authorities, active labour market policy and regional policy

  - Reconcile social groups, ethnic differences, solidarity

  - Involvement of citizens

  - Territorial Cooperation

How to stimulate further?

- Cohesion Policies should revive their explorative and innovative character ➔ stimulate experimental policies . Allow eventually for failures.
- Animation and training for changing practices and routines - Focus on changes in attitudes and behaviour
- Support approaches with new policy orientation (return to Community Initiatives?)
- Introduce proportionality between purpose, scale and type of intervention and implementation rules!

Policy conclusions

2 ways to think about the new Cohesion Policy

A penny saved is a penny earned, and a lot of saved pennies can accumulate to a significant sum

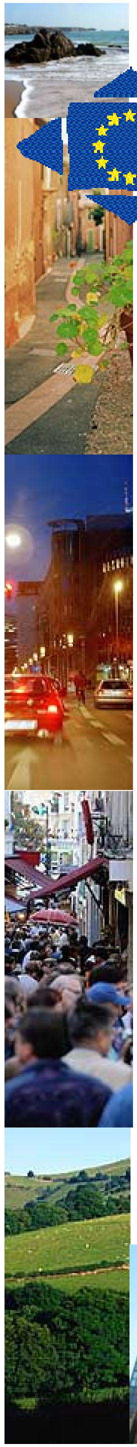
Benjamin Franklin

Give me but one firm spot on which to stand,
and I will move the earth

Archimedes

Can we appreciate leverage effects also in other EU policies?

- Financial leverage and PPPs
- Strategic policy orientation
- Institutional capacity building
- More cohesive Europe



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Thank you

What should be the redistributive function of the EU budget?
Prof. Daniel Tarschys

1. My brutal answer would be: none whatsoever.
2. This does not mean that I am against redistribution, solidarity and social policy. On the contrary. The market economy can survive and flourish only if it is accompanied by a broad range of measures intended to equalise living conditions between the workforce and those not yet or no longer in it, and those who have never been on the labour market for reasons of disabilities. Modern society needs social insurance protection and a wide spectrum of social services.
3. But then comes the question: who does what? Musgravian economics assigns three tasks to the budget: allocation, redistribution and stabilisation. Fine, but every budget need not do all of these things. A budget handling only about 1 percent of our GDP, or around 2,5 percent of our total public spending, should focus as much as possible on allocation, leaving the other two to lower levels of governance.
4. The EU (and Euroland) may play an important role in stabilisation policy, but not through its own budget. Its arena of action is rather the coordination function that can be exercised through the broad economic policy guidelines and the measures taken to assure compliance with the obligations that the Member States have assumed to observe public finance discipline.
5. As far as redistribution is concerned, the Member States make considerable efforts along several dimensions and are also remarkably successful in attaining i.a. geographical equalisation. If the gross disparities before taxes and public expenditures are compared to the net disparities after these public interventions, we will find that territorial differences shrink to about half their original size.
6. This also means that regional disparities are much smaller than normally assumed in the EU statistics. EU structural policy as a whole is based on a significant exaggeration of the real economic gaps.
7. EU resources are best used for collective European goods and services and, in the many cases where there is a mixture of public and private benefits, for purposes where the collective element is as substantial as possible, and where this element spans across borders. There are many under-funded needs of this kind, so our ministers of finance should not hope to recover anything at all from the substantial savings possible in CAP and structural policy. Examples of worthwhile common endeavours are easy to find in such areas as research, internal and external security, neighbourhood policy, environment and climate policy.
8. The Member States are of course obsessed with their net flows. In my view the best EU expenditures are those where a net flow cannot even be calculated, because of the widely shared benefits. If a net benefit can be observed I would rather see that as a good reason to check whether EU money is really used for appropriate purposes.
9. But what about the poor and lagging countries and regions? Isn't very important to support their development? No doubt. But the main benefits of EU membership for these areas are not to be found in subsidies but in the access to wider markets and to a broad range of other, often regulatory benefits linked to the Union. Support for institution-building should continue, as should support for cross-border investments and activities. But when it comes to other public investments with predominantly domestic relevance, that field should be left largely to domestic decision-makers and budgets.
10. In the EU context, the term "cohesion" has been converted into a label for redistributive measures with little proven effect on real cohesion in the original meaning of that word. The concept should be reclaimed and applied to policies with potentials to extend a genuine sense of community in Europe or, if you wish, a European identity. That kind of policy will to a large extent be found in such areas as education, culture, mass communication, research, human encounters and mobility.

The EU Budget as an instrument of redistribution

Prof. em. .VAN GINDERACHTER

1.Just 30 years ago – in April 1977 - the MacDougall report suggested a EU budget of 2 – 2.5 % of GDP in order to reach a pre-federal structure. Today there is at most political support for a budget f 1% of GDP.

2.Under those circumstances there is hardly any room in the EU budget for a stabilisation function.
On the contrary there is a limited possibility for allocation: foster Community priorities in R§D, transport, environment, external relations, internal security, and, of course, agriculture.
The bulk of the EU budget - some 50 % - should be used for redistribution purposes.

3.Experience of the last 30 years has demonstrated that with such a limited budget a well designed strategy can perform miracles in cohesion policy (Ireland and Portugal).

4.Apart from ethical and social arguments ' to ensure the harmonious development (of their economies) by reducing the differences existing between the various regions and the case of the less-favoured regions' there are also economic reasons to promote economic and social cohesion. By providing basic infrastructure and vocational training total production and overall productivity can be significantly increased in activating idle capacity.
There is no contradiction between promoting both competitiveness and cohesion.

5. Every 7 years there should be a thorough evaluation of the policy impact reached and the targets to be set for the next period. Transparent criteria of countries and regions eligible for assistance should be maintained. Clear EU priorities should be set for national programmes to be introduced.
Permanent monitoring – financial and economic – are of paramount importance.

The new own resources

Prof. em. J.VAN GINDERACHTER

1.It is inappropriate to spend every 7 years months of negotiations within the EU institutions and hours of bargaining between heads of state and government to reach a (mostly inconsistent) deal for the EU financial perspectives for an amount of only 1 % of GDP.

2.Instead of national contributions for 70 % of the EU budget the own resources system should be restored in an as simple way as possible: beyond the agricultural levies and the custom duties on industrial products the EU budget should be financed by e.g. a EU share of excise duties (in €/litter fuel and/or petrol), the condition of course being that the overall fiscal burden should remain unchanged for all EU citizens. One could also think of a EU kerosene tax. Anyway those very visible- own resources should replace the (theoretical) VAT contributions as well as the transfers from the national budgets.

3. There should be an overall correction mechanism installed along the lines proposed by the Commission:

- no member state should have to support a net contribution above 0.35 % of its GDP;
- if that level is reached there should be an automatic compensation of 66 %.

4. The existing dichotomy between a priory fixed resources and yearly expenditure voted by the Parliament should be abolished: responsibility for both resources and expenditure should be given to both Council and Parliament to be decided possibly with a (super) qualified majority.
The rule 'no taxation without representation' should be fully respected in EU institutions as well..