S&D

Group of the Progressive Alliance of
Socialists & Democrats
in the European Parliament

European Parliament
Rue Wiertz 60
B-1047 Bruxelles
T +32 2 284 2111
F +32 2 230 6664
www.socialistsanddemocrats.eu

Reform of the System of Own Resources of the EU for the 2021-2027 Multiannual Financial Framework

Position paper for the 2019-2024 legislative term

"The Union shall provide itself with the means necessary to attain its objectives and carry through its policies. Without prejudice to other revenue, the budget shall be financed wholly from own resources"

art. 311 TFUE

I. Ground for revision

Over the past few years and months, the EU has been facing a growing number of unprecedented challenges, including the COVID-19 pandemic with its disastrous consequences for the economies and societies of the affected Member States, the previous financial crisis, which provoked a rise of youth unemployment and inequality, climate change and the arrival of new migratory flows from the less developed regions of the world, to name a few. In such a context, the 2014-2020 EU Multiannual Financial Framework (MFF) has shown its limits, due to its modest financial resources, which have proven to be insufficient to allow the Union to effectively deal with the current international setting. As a negative consequence, the European Commission has been resorting to precarious and borderline solutions, such as the creation of financial instruments outside of the scope of the EU budget, for which the European Parliament has limited power of scrutiny, as well as the inefficient practice of redeploying funds between political priorities. The negotiations on the 2021-27 MFF, conducted in the middle of a huge recession caused by the Covid19 emergency, in parallel with those on the Recovery Plan, have shown the importance of discussing the future financing of the European project itself.

Moreover, this already difficult situation has been worsened by the narrow approach that European Ministers of Finance adopt in the EU annual budgetary negotiations, in which case, decisions within Council are taken according to the logic of the "zero sum game", with the objective of saving as much money as possible for national budgets, while ignoring the specific

European added value of pursuing common programmes and objectives at the EU level. The reasons behind this misconception lay in the recent times evolution of the financing mix that characterizes the revenue side of the EU budget: from 1988 to 2014, the share of own resources (i.e. VAT, custom duties, sugar levies, etc.) within the EU budget decreased from 85% to 23% at the advantage of GNI based contributions, which, although labelled as "residual source of revenue" by the Treaties[1], went up from 11% to 69% during the same period. This unfortunate development led to a condition in which the EU budget, mostly hostage of negotiations between Member States in the EU annual budgetary procedure, often ends up being endowed with insufficient resources that do not allow the Union to accomplish its policy objectives. In other words, the more and more prevailing "GNI based contributions approach" strengthens the inter-governmental dimension of the European institutions to the full disadvantage of a genuine European integration process and a stronger Union.

The concept of added-value creation excludes the "zero sum game" and "juste retour" routines, as defended by many capitals. Hence, the purpose of the EU budget is to address areas that are a priority for the EU and where the taxpayers' money spent at EU level create more and better public goods, compared to the public funds spending at national level. To accomplish this task, the EU budget must observe the principles of efficiency, effectiveness, transparency, unity and redistribution, as well as have the adequate size for fulfilling the political commitments of the Union and the flexibility needed to respond to unforeseen situations.

In order to find a solution to the shortcomings of the current financing system, the three institutions agreed to establish the High Level Group on Own Resources, led by Mario Monti, with the mission of analysing possible scenarios for an efficient reform of the revenue side in line with the principles mentioned above, i.e. simplification, transparency and democratic accountability. The final report of the High Level Group, published in January 2017, puts forward a list of nine recommendations[2] that question the appropriateness of the current revenue side and launch new ideas for the reform of the post-2020 system of own resources.

II. Agenda for a change: S&D vision for the post-2020 revenue architecture

i. An ambitious basket of new own resources

The EU must reclaim ownership over its budget and policy agenda. The current mix of revenue financing the EU budget, which consists of GNI contributions by approximately 70%, has led to a situation in which the European project itself lacks its own operational legitimacy and is mostly dependent on budgetary decisions taken by Member States. In this context, as said before, the worst outcome is the "zero sum game" logic that predominates in budgetary

[1] According to the Treaties, GNI contributions have a balancing function, since any increase in other sources of revenue or the introduction of new own resources will automatically entail a corresponding reduction in the GNI based share of the budget.

[2] The nine recommendations from the High Level Group are available in the EU budget section of the website of the European Commission (ec.europa.eu).

negotiations within Council, where the main objective of finance Ministers is to bring back to national budgets as much money as possible.

The S&D Group considers **the introduction of a basket of new own resources, whose tax bases shall be linked to the implementation of EU policies** converging towards the overall objective of smart, sustainable and inclusive growth**, as a crucial element of the reform**. More specifically, new revenue shall stem from measures addressing both the **protection of the environment** and the **promotion of a fairer internal market.**

In addition, the Group demands the establishment of the general principle that **future revenues generated by the implementation of EU policies shall flow in the EU budget as own resources** (at least in specific fields, such as environment, internal market and anti-money laundering). In line with the same view, the **EU should increase the integration of its fiscal policies, thus establishing its autonomous fiscal capacity and be more resilient in the fight against tax avoidance**. This would gradually produce a genuine fiscal Union, beside the monetary Union, which is not alone sufficient to guarantee a strong and credible Europe.

This financial boost shall result in a proportionate reduction of the share of GNI contributions down to 40% of total financing, increasing the EU's financial autonomy and thus improving its ability to deliver on citizens' expectations.

Moreover, due to the global Covid19 social and economic crisis, the idea of mainly relying on national contributions cannot work anymore, since the member states' GDP, although with some differences, is expected to dramatically fall; we need to invert the logic and to build on the crisis to introduce significant and genuine European own resources in order to support with an adequate tools box the recovery and avoid new economic divergences. The new revenue mix will - in fact - not only allow the Union to increase its degree of budgetary independence from Member States' national budget restrictions, but also to take its own course of action in global politics.

Therefore, in line with the recommendations of the Monti Report, as well as with the parliamentary resolutions adopted in the 2014-2019 mandate and in the current legislative term, the S&D Group demands the introduction of a basket of new own resources consisting of a broad variety of sources of revenue, with the objective of differentiating the risk generated by possible shortfalls deriving from their implementation:

- **the auction revenues of the EU Emission Trading Scheme (ETS)**, whose objective is to reduce CO2 emissions generated by the industrial sector. The revenue generated by these allowances is expected to progressively decrease in the long term with the adoption of cleaner manufacturing processes. In parallel, after a thorough impact assessment, S&D is ready to consider the extension of the scheme to other sectors, such as the maritime one. As for aviation, the number of free allowances shall be gradually phased out with the objective of overhauling the ETS according to a full auctioning approach, in line with the polluter pays principle: this provision will guarantee revenue increase in the short and medium term. The ETS could raise from 3 to 10 billion € per year[3], depending on variations in the carbon price and the extension of the system to other sectors;

[3] European Commission, 2020, the EU budget powering the recovery plan for Europe".

- **a Contribution on Non-Recycled Plastic Packaging**, whose purpose is to encourage EU citizens to embrace alternative green practices; as a consequence, its income is expected to decrease over the time. This contribution could generate around 7 billion € on an annual basis[4];
- **a Carbon Border Adjustment Mechanism**, that could ensure a level playing field in international trade, reduce the off-shoring of production and incorporate the costs of emissions in the prices of imported goods. This mechanism shall at the same time respect the principle of free and fair global trade, and shall not be a prerogative for the EU to foster protectionism vis-à-vis third countries. The generated income, estimated to amount from 27 to 84 billion € per year[5] depending on the design of the mechanism, is expected to progressively decrease with the adoption of cleaner manufacturing processes, which remains the main aim of this initiative;
- **a Corporate Income Tax revenue based on a Common Consolidated Corporate Tax Base (CCCTB),** targeting large companies, including multinational companies harbouring their profits in fiscal havens, while not impacting SMEs. Such a measure would reduce tax evasion, fiscal competition among Member States, facilitate cross border trade and tap resources from the added value created by the single market. A share of revenue based on a solid CCCTB is estimated to generate a substantial contribution, which could amount to around 75 billion € per year[6];
- **a Digital Service Tax,** targeting large companies whose intangible profits are not easily identifiable by current national taxation systems and can be moved across the Single Market and beyond. In this way, highly digitalized companies easily gain a tax advantage before their competitors and therefore a fiscal intervention would be required. Revenue could either be based on a share of the "unified approach" to tax digitalized businesses, as agreed at global stage, or an EU own solution to tax digital giants. To be noted that in the period of the lockdown due to the 2020 pandemic, the whole Europe goes online and the biggest digital companies are expected to make huge profits, more than ever before. Such a tax could raise 5 billion € annually[7];
- **a Financial Transaction Tax (FTT)**, to be implemented according to an efficient scheme agreed among all Member States. This measure would mitigate tax competition, contribute to the fight against tax evasion and fraud, as well as reduce the number of destabilizing transactions in the context of high frequency trading. An FTT based on the current participation of ten Member States would produce around 3.5 billion € per year[8], while a scheme envisaging the involvement of all Member States could generate,

European Commission, 2018, "Own Resources for 2021-2027".

[4] European Commission, 2018, "Own Resources for 2021-2027".

[5] Margit Schratzenstaller, 2018, "Tax-based Own Resources as a Core Element of a Future-Oriented Design of the EU System of Own Resources".

[6] Danuše Nerudová, Veronika Solilová, 2019, "The Impact of the Introduction of a CCCTB in the EU".

[7] European Commission, 2018, "Fair taxation of the digital economy".

[8] KPMG, 2019, "German Finance Minister issues amended Financial Transaction Tax proposal".

depending on its structure, a more meaningful contribution, ranging from 25 to 81 billion € annually[9].

In addition, S&D calls for the adoption of the following sources of revenue to finance the EU budget:

- **a European Net Wealth tax for the richest segment of the population**, that could address excessive wealth inequality. An EU-wide implementation of a wealth tax based on harmonised tax provisions would limit the risk of tax avoidance by wealthy individuals across the EU. Such a tax would be addressed to the highest segment of the population in terms of individual net wealth. Given the European nature of such a tax, it could substantially contribute as an own resource for the EU budget. A small European contribution on the 1-1,5% of wealthiest individuals could raise, according to some estimates, up to 150 billion € per year in total[10];

- **a Single Market Levy**, in the form of a subscription for companies to participate in the Single Market. Such a levy would be implemented according to lump sum contributions, the amount of which would vary according to companies' turnover. Small companies shall be exempt. In addition, a Single Market Levy could be applied as an interim solution before the adoption of the CCCTB. Such a contribution would bring around 10 billion € to the EU budget on an annual basis, depending on its design[11];

- **Revenue from the European Central Bank**, generated by the issuing of currency and the presence of deposits. Currently, these profits are collected by the ECB and mostly distributed among the central banks of the Member States of the Euro Area. An own resource for the EU budget based on this revenue could be used to finance initiatives limited in scope to the participants of the Euro Area and could take the form of a fiscal capacity. The total annual income produced by ECB profits has been very volatile in recent years, fluctuating from 10 to 25 billion €[12].

The above-mentioned own resources do not only generate income for the EU budget, but they also have the potential to correct negative externalities and market failures. As such, it should be noted that some of these resources, with specific regard to the ones linked to environmental measures, are meant to decrease and hopefully disappear over the time, in parallel with the replacement of traditional practices with sustainable alternatives by EU contributors. Therefore, to ensure the reliability of the EU budget and the continuity of EU policies, the Group should

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[9] According to Nerudová (D. Nerudová, M. Schratzenstaller, V. Solilová, The Financial Transactions Tax as Tax-based Own Resource for the EU Budget, FairTax Policy Brief No. 2, 2017) potential revenues go from 25 to 33 bl € per year; but the Commission in 2012 proposes up to 81 billion €, even though including the UK (European Commission, 2012, "The financial transaction tax will reduce Member States' GNI contributions to the EU budget by 50%".)

[10] Margit Schratzenstaller, 2018, "Tax-based Own Resources as a Core Element of a Future-Oriented Design of the EU System of Own Resources".

[11] European Commission, 2020, the EU budget powering the recovery plan for Europe".

[12] High Level Group on Own Resources, 2016, "Final report and Recommendations".

focus in parallel on the adoption of more stable sources of revenue produced by the functioning of the internal market, as previously listed.

Funding generated by new own resources shall flow into the EU budget as general revenue without being earmarked for specific programmes. This approach would provide the EU budget with the necessary resources and flexibility to respond to unforeseen challenges, like the one for instance of the 2020 health emergency.

ii. A more accountable EU budget: the abolition of rebates

The departure of the UK from the Union and the consequent **removal of the British rebate offers the opportunity to renegotiate and eliminate all the related correction mechanisms granted to Germany, Austria, Denmark, Sweden and the Netherlands.**

The EU budget must be built on a simpler, fairer and more transparent structure. It has to be democratically accountable and "user-friendly": citizens of all the Member States must be in the condition to read it and understand where their money comes from and what it is used for. The calculation of national rebates has been criticised for its opaqueness and lack of transparency, making it very difficult for citizens to catch the connections between EU revenues and expenditures.

The S&D Group shares the position presented by 18 Member States in October 2019, which clearly explained why **the two conditions that applied to the UK for supporting the introduction of rebates, as set in the European Council conclusions of Fontainebleau in 1984, are no more in place:**

- expenditure mix of the EU budget with the dominance of a single policy: at that time, expenditure in agricultural policy accounted for more than 2/3 of the total financing and the UK, not agriculture oriented as other Member States, was penalized; in the Commission proposal for the 2021-2027 MFF there is no dominant policy and CAP counts less than 30% of the total MFF expenditure;
- a Member State's budgetary burden exceeding its relative prosperity: both the distance from the average GDP and the budgetary burden were much wider for the UK at that time; today, all the Member States benefitting from corrections are among the more developed ones and they contribute in terms of GNI less than most Member States.

With respect to financial gains, the removal of the above-mentioned rebates will approximately result in additional 5 billion € for the EU budget on an annual basis[13].

iii. An ambitious budget for facing new challenges

The Union must be endowed with a stronger and more ambitious budget, critical for winning new challenges and pursuing its policy objectives. **The own resources ceilings for commitments and payments, currently set at 1.26% and 1.20% of EU GNI respectively, shall be brought up**

[13] Estimation provided by Xavier Ragot, Research Director at the French National Centre for Scientific Research.

to values reaching the 2 or even 3% in order to allow the EU to rely on a bigger budget for the fulfilment of its political ambitions. In addition, such a permanent increase shall allow to create sufficient headroom between the MFF ceilings and the own resources ceilings, whose capacity can be technically used to borrow money on the financial markets and issue European common debt guaranteed by the EU budget, in case of need. Such a feature would characterize the foundations of any credible Recovery Plan, which shall allow to avoid the mistakes of the aftermath of the 2008 financial crisis. A new set of robust own resources for Europe would make public budgets and social safety nets stronger by raising revenue at EU level that could not be generated at national level. A smarter budget would draw resources from the increased European added value and public goods it creates.

In addition, the internal cohesion of the EU budget shall be strengthened, according to the principle of budgetary unity. The existing funds and financial instruments have to be gathered under the democratic control of the European Parliament. Financial instruments outside the budget can be a temporary solution to increase funding but cannot become a replacement for EU resources, dedicated to closing the division gaps between Member States and citizens.

III. A strategy for negotiations

Taking into account that, in the framework of MFF negotiations, the Parliament has only power of consultation over the main Commission proposal on the system of own resources, S&D made clear, in the context of the adopted parliamentary resolutions, that **no agreement will be reached on the 2021-2027 MFF, for which the Parliament has to give its consent[14], without the due inclusion in the final deal of the group's demands with regard to the reconfiguration of own resources**. This approach, that can be generally adopted in MFF interinstitutional talks, would allow the Parliament to obtain leverage power when negotiating with the Council and the Commission.

In addition, the regulation laying down implementing measures for the system of own resources, for which the Parliament has power of consent, is extremely relevant, since it establishes the uniform call rates for the collection of new own resources. S&D could impose an increase in the call rates, implying a corresponding reduction in the share of GNI contributions to the EU budget, as a red line in negotiations.

In general terms, with respect to the revision of the EU treaties, S&D calls for the **modification of article 311 TFEU, with the objective of reinforcing Parliament's role in the decision-making process for the adoption of the upcoming Own Resources Decisions**; both arms of the budgetary authority, Parliament and Council, shall act as co-legislators endowed with equal powers when negotiating the revision of the system of own resources of the EU. Also, the implementation of the Interinstitutional Agreements that safeguard Parliament's prerogatives should be closely monitored and further developed, with the objective of conferring adequate

[14] Consent by majority of Parliament's component Members.

decision and scrutiny power to a democratically elected EU Institution and budgetary authority over the revenue side of the EU budget.

As concerns the decision-making process within the **Council**, while valuing the consensus-oriented approach, in case of long-lasting negotiations leading to protracted blockage and veto points, this institution **shall be able to take decisions on the domain of own resources by qualified majority voting**, by initially activating the passerelle clauses in the Lisbon Treaty.

With the objective of increasing the chances of success with regard this ambitious reform, the S&D Group shall also resort to the following measures:

- building strong relations with the socialist Ministers and Commissioners via the S&D contacts in the PES and intensifying inter-institutional talks with the Council and the Commission;
- promoting the discussion on the reform of the own resources in the framework of the negotiations of the Recovery Plan, the Green Deal, the Just Transition and the industrial strategy;
- enhancing dialogue with national parliaments with the aim of involving them in the reform process, by making clear that new own resources will not require additional financial efforts by Member States but rather the implementation of policies that no country could pursue by itself;
- reaching out to European citizens through a strong S&D communication strategy in order to counter disinformation;
- encouraging the revision of own resources and Parliament's power over the revenue side of the EU budget as a "constitutional" change within the Conference on the Future of Europe;
- involving the rising climate movements in this strategy: the rising awareness and mobilisation among our citizens on climate change should be seen as an opportunity for the revision of the EU system of own resources. To be noted that revenues connected to the fight of climate change are the ones that are mostly legitimised by public opinion.

This is the time to steer the destiny of our Union towards a more sustainable future. The economic crisis, due to the worldwide 2020 pandemic, has made clear that we need a stronger Union. The new Green Deal and the implementation of the Social Pillar have to be pursued as well, with an ambitious and innovative approach, based on a strong and fair fiscal capacity. We have to provide the EU with suitable means for its priorities and unforeseen challenges, in order to meet the rising expectations of EU citizens, not only in the short but in the long run. Acting now is the only way to preserve the European community in the future.