

A stylized world map composed of a grid of grey dots, with several dots highlighted in red to represent specific countries or regions.

An EU Tax

Overdue Reform or Federalist Fantasy?

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- Calls for genuine EU taxes to provide the bulk of the EU's revenue have been frequently heard over the years, but just as frequently rejected. The completion of the budget review of the current Medium-term Financial Framework has stimulated fresh debate on this matter. In particular, the idea of using a financial transactions tax to fund EU spending has captured attention.
- As a technical proposition, there is no over-arching obstacle to an EU tax and there are plenty of options that could be viable, with variants on energy taxes or corporate income tax among the favourites. But there is unlikely ever to be a contender that is *the* ideal EU tax, because any conceivable instrument will have attributes that someone will oppose. And it should not be overlooked that the current own resources system, based predominantly on national contributions, has a number of advantages.
- Neither citizens nor Member State governments will be easily convinced that any EU tax makes sense, yet its likely impact should not be over-stated. It will not, on its own, resolve the intractable problems of net balances and the resulting corrections, but it might help to lessen the acrimony surrounding the issue. Nor will giving the EU more autonomy in revenue raising precipitate a federal super-state, although it would be more consistent with the Treaty.
- The aim of this paper is to look behind the often rather strident politics and to investigate the case for an EU tax analytically. The paper proposes and assesses criteria for selecting potential taxes, and looks in detail at a number of options for new funding instruments. It then appraises the scope for significant change in how the EU budget is financed and how it might be achieved.



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Introduction

Howls of outrage from several national capitals greeted the rather mild suggestion (in an interview with *FT Deutschland* published on 9 August 2010) from Janusz Lewandowski, European Commissioner responsible for the EU budget, that some form of EU tax should be introduced to finance at least part of EU expenditure beyond 2013. For example, Pierre Lellouche, then France's Europe Minister, deployed his customary flamboyant rhetoric to adjudge the idea »*parfaitement inopportune*«. Further condemnation of the idea followed the long-delayed publication of the Commission's Budget Review, with Chancellor Merkel expressing her measured, but equally implacable opposition following a meeting with Belgian Prime Minister Leterme. In response to a very direct question at a press conference she said: »Wenn Sie mich so klar fragen, dann sage ich, dass ich dagegen bin, dass eine EU-Steuer eingeführt wird« [Since you ask me such a clear question, let me say that I am against the introduction of an EU tax].¹

But the irony is that, since 1971, the EU *has* had its own taxes in the form of customs duties and agricultural levies that are assigned directly to the financing of the EU budget. Indeed, they are now described as the »traditional« own resources and accounted at their peak in the 1970s for more than half the EU's revenue. It follows that objections to the principle of EU taxes have already been overcome and it must therefore be political factors that lie behind opposition to greater resort to them. Since the mid-1970s, the trend has been for a growing proportion of the EU's funding to come from direct payments from the Member States, rather than identifiable EU resources, and successive attempts to introduce new EU resources have rapidly been rebuffed.

This paper sets out the formal position on how the EU is funded, reviews the arguments for and against EU taxes, discusses criteria for selecting potential taxes and looks in detail at a number of options for new funding instruments. A concluding section then assesses the scope for significant change in how the EU budget is financed and how it might be achieved.

1. Available at: <http://www.bundesregierung.de/Content/DE/Mitschrift/Pressekonferenzen/2010/11/2010-11-02-pk-bk-leterne,layoutVariant=Druckansicht.html>

1. How the EU budget is financed

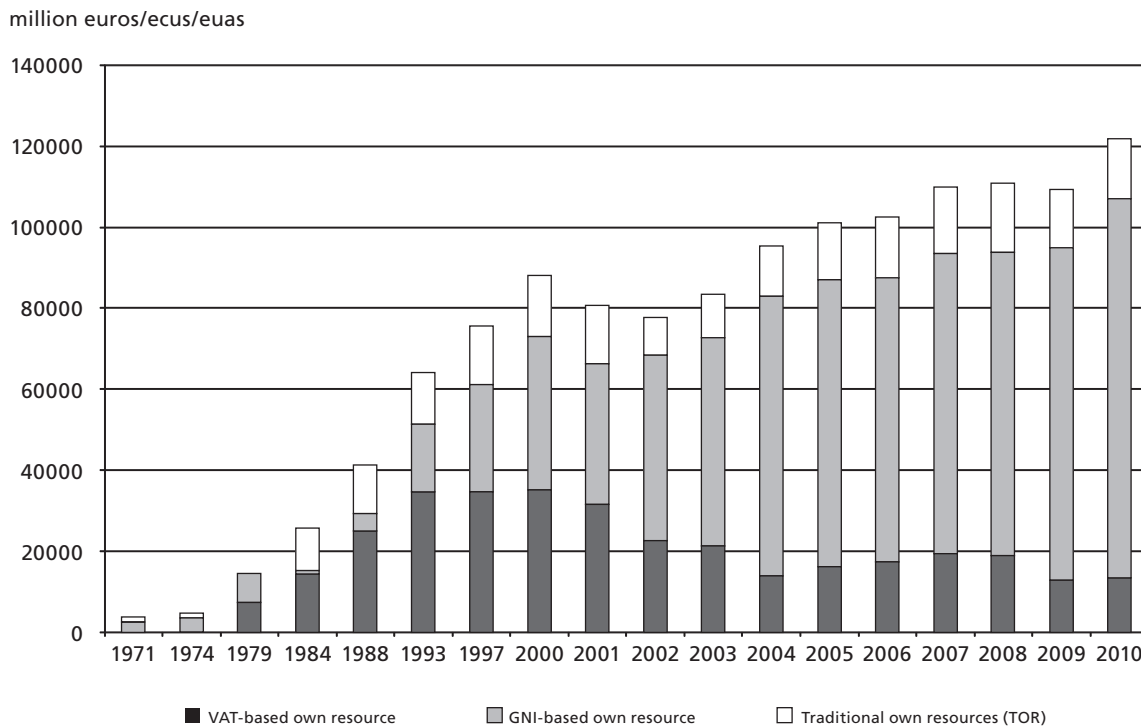
The financing of the EU's spending has evolved considerably over the years and, even though the budget is barely two per cent of aggregate public expenditure by general government in the EU as a whole, has been a source of considerable friction. The constitutional position is very straightforward: Article 311 (TFEU) states unambiguously that »without prejudice to other revenue, the budget shall be financed wholly from own resources«. This formulation is unchanged from previous versions of the Treaty, although Article 311 is a little more prescriptive than its predecessor versions in going on to state that the Council »may establish new categories of own resources or abolish an existing category«. The obvious interpretation is that there is no constitutional obstacle to explicit EU taxes or, for that matter, using other revenue streams. The Treaty also stipulates that the EU budget must always balance.

Today, the EU budget is funded by four own resources that have been in place since the last major reform of the EU budget, in 1988. In strictly legal terms, these resources, which are enshrined in the *Own Resources Decision* ratified by all 27 Member States, are »owned« by the EU level. This decision, last formally agreed in April 2007 and remaining in force, gives the EU a legally binding right to receive the revenue emanating from these resources. They are:

- The proceeds from agricultural levies and customs duties collected by Member States as agents for the European Commission. These are known as the »traditional own resources« (TOR) because they date from 1971 when the notion of own resources was introduced. They generated a fairly substantial proportion of total EU revenue in the mid-1970s, but the lowering of tariffs and other reforms have eroded the tax base.

- A proportion of the VAT collected by Member States, based on a take-up rate that was initially set at one percentage point of national VAT, but has since been cut to 0.3 per cent (with lower take-up rates for some Member States, rationalised as a means of giving them rebates). The VAT receipts are corrected to reflect differences in national rates and coverage of the tax, so that they do not directly flow from the VAT collected.

Figure 1 Evolution of own resources since their introduction in 1971



Source: European Commission, DG Budget.

■ A resource proportional to the gross national income (GNI) of Member States. This fourth resource has the property that it varies depending on the yield of the first three resources such that EU revenue exactly matches EU expenditure, thereby facilitating the attainment of balance. This residual property is an important facet of the fourth resource.

In the EU's accounts, the VAT and GNI resources are presented as national contributions, whereas the TOR are regarded as direct community revenue (and thus, de facto, as EU taxes). The yields of the different resources have fluctuated considerably since the establishment of the own resources system in 1971, but the clear trend has been for an increasing proportion to come from the GNI resource. The steady increase in the share of the national contributions (the VAT resource and the GNI resource) relative to the TOR can readily be seen from Figure 1.

Prior to the introduction of own resources, the then EEC had been funded exclusively by national contributions. Between 1971 and 1979, when the VAT resource was

introduced, the TOR became the largest contribution to total revenue, reaching a peak share in 1974. The VAT resource provided the largest share from 1979 until the late 1990s, after which the GNI resource became the main funding stream. The projected share of the GNI resource for 2010 and 2011 is up to three-quarters. Together, the VAT resource and the GNI resource now comprise nearly 90 per cent of own resources.

The Commission has proposed, in its budget review communication, to abolish the VAT resource on the grounds that the need to correct for national differences in coverage and rates, as well as levels of prosperity, makes it effectively a second GNI resource. Consequently, persevering with a separate VAT resource serves only to render the system of own resources more complex and opaque. As there is little support for retaining it from the Member States, this proposal is likely to be accepted. Assuming EU spending – and thus the revenue-raising requirement – stays at about one per cent of GNI in the period beyond 2013, when the current Multi-annual Financial Framework will have to be renewed, the implication is that the GNI resource would remain at 90 per

cent or above of total own resources for the foreseeable future. The question that then arises is whether what is, in several respects, a satisfactory means of financing EU expenditure can be sustained in the face of criticisms that national contributions should not be so dominant.

1.1 Strengths and weaknesses of the current system

A great strength of the current system is that it works. The EU budget is assured of its income, so that the European Commission does not have to fret about how to raise income to finance its expenditure commitments. Through the operation of the GNI resource, the system also ensures that the EU budget will always balance, because of the feature that the call on the GNI resource is deliberately designed to be just enough to match spending. The current system of revenue raising is also tolerably fair in the burden it imposes on Member States, since its starting point is that each should pay, *ex ante*, roughly one per cent of its GNI to the EU. What each pays *ex post* is a different matter because the gross contributions of a number of Member States are reduced through a variety of correction mechanisms – the UK abatement and the many other devices used to reduce the net payments of certain Member States.

Consequently, it is no surprise that many of the main battles on the revenue side are about »corrections«. It is important to be clear that it is unbalanced EU spending that motivates demand for these corrections. Member States at similar levels of prosperity can receive very different amounts of EU spending per capita because of how certain EU policies – above all, but not only, agricultural policy – function. Although the convention is to place most of the corrections (notably the UK abatement, the lower take up rates of the VAT and GNI resources granted to Austria, Germany, the Netherlands and Sweden), on the revenue side of the EU budget, they are a problem that is linked only indirectly to the specific instruments used to fund the EU.

In particular, a number of commentators argue that because it is national finance ministries that have to make the monthly payments of the national contributions, they are then led to focus much more closely on the net balance position. The corollary is that if the EU budget were funded by own taxes, what Jacques Le Cacheux (2005) has described as the »poisonous« *juste retour* emphasis

in everything to do with the EU budget would be diminished. It is certainly true that such a mentality is damaging and can induce negotiators to prefer policies that boost »their money back« rather than those that Europe needs. But with the net balance genie out of the bottle, it is far from obvious that substituting national contributions by a new EU tax would solve the problem. In any case, the first question that would be posed (whether by tabloid newspapers like *Bild* in Germany or the *Daily Mail* in the UK, or by national political leaders) about any proposed alternative to the current system would be: »what will it cost us?«

That said, other criticisms of the existing system also stem from overtly political aims or concerns, rather than the more banal issue of how straightforward it is to raise sufficient finance. Both the Commission and the European Parliament believe that the EU level should have greater autonomy in fund-raising, often presenting the argument in terms of connecting how the EU is funded to the policies it pursues. The Parliament has also emphasised that the visibility and transparency of EU funding matters and some leading MEPs maintain that the present system is too easily obfuscated in a way that encourages myths about the burdens imposed on Member States or citizens. Another consideration is constitutional: are national contributions consistent with the spirit of Article 311 of the Treaty? It is a matter of judgement what should count as an authentic own resource, but in an economic sense the national contributions fall short of being genuinely own resources (or taxes) that »belong« as of right to the EU level. Instead, they have the character more of inter-governmental transfers. Box 1 provides a brief overview of »own taxes«.

Box 1 The notion of own taxes

There is an extensive public finance literature on »own taxes«² which can be summarised under a number of headings, although the gist of an own tax is that it is one over which the government in question exercises autonomy. Questions that arise include where responsibility lies for determining the scope of the tax, setting its rate and collecting it, as well as which level of government receives the proceeds of the tax. In multi-level systems, the federal or central government often acts (for efficiency reasons) as the agent for collecting and distributing the tax, even if the revenue is assigned to sub-national levels. Indeed, in the EU, the collection of traditional own resources (TOR) is done by national administrations (which are given a collection fee currently set at 25 per cent of the revenue³). In practice, therefore, autonomy is a fuzzy concept, implying that there are degrees to which a tax can be said to be »owned« by a government.

However, there are certain properties of own taxes that are worth mentioning. A conclusion from the

academic literature – especially what is known as second generation fiscal federalism – is that the obligation to raise revenue aligns incentives better for a budgetary entity (Weingast 2006). The reasoning is that transfers offer few inducements to tailor public expenditure to citizens' preferences, that they lead governments to focus on maximising the transfer and not to pay heed to what is spent and that they also undermine democratic control. The argument is usually framed for sub-national governments in relation to central government (much of the literature emanates from students of federal systems), but could reasonably also be applied to the relationship between the national and EU levels. This would imply a meaningful say for the European Parliament in revenue raising, something that it did not gain from the Lisbon Treaty, despite its advances in other domains (including acquiring an enhanced role in shaping EU spending).

2. Choosing a suitable EU funding instrument

Any means of financing the EU budget has to meet a number of expectations, several of which pull in different directions. Indeed, choices on funding instruments for any political entity require a careful balancing of different considerations and, thus, a focus on the normative dimension. Some of these considerations derive from tax theory which identifies principles such as ability to pay, economic efficiency and equity as desirable in any funding instrument. Some are more directly administrative, examples being ease and cost of collection, or stability and sufficiency of revenue. Others still, in the often highly-politicised EU context, concern political imperatives, ranging from connections to EU goals and policies to transparency.

2. For a comprehensive overview, see Bird (2000).

3. Prior to the agreement of the EU's 2000–2006 Multi-annual Financial Framework and the associated »Own Resources Decision« the fee was 10 per cent. The increase to 25 per cent can best be understood as a device to give a rebate to the Netherlands which collects a disproportionate share of the revenue because a high share of imports enter the EU through Dutch ports.

The criteria which might, in principle, be considered relevant were discussed at length in a background study done for DG Budget of the Commission as part of the 2008/9 budget review by Begg, Enderlein, Le Cacheux and Mrak (2008). This analysis put forward a comprehensive list of factors most likely to matter to EU citizens and decision-makers. These are summarised in Table 1, which elaborates on the corresponding table from the report, and can serve as a template for discussing the arguments for and against changing the current system.

2.1 Dominant or »veto« criteria

Some criteria are inevitably going to be more salient than others and it can even be argued that »red lines« may be drawn around some of them. In particular, much of the opposition to an EU tax is about denying autonomy to the EU level in revenue raising, with several Member States resolutely against any loss of their power to tax. Seen in this way, the national contributions are a vital control mechanism that Member States will be reluctant to cede, irrespective of other arguments in favour of EU

Table 1 Criteria for assessing potential EU own resources

Criterion	Explanation
Economic considerations	Criteria that reflect analytic factors derived from economic theory or tax theory
1. Economic efficiency/distortion effects	Does the resource affect only some sectors of economic activity? If the tax or levy leads to a distortion of demand, this is usually considered to be undesirable, insofar as it results in a sub-optimal allocation of resources. However, in the case of »Pigouvian« taxes, the allocative effects may be positive if they deter harmful or otherwise undesirable economic activity.
2. Vertical equity in promoting redistribution	The principle of ability to pay is usually that proportionally more should come from richer citizens (a progressive tax), thereby achieving some net redistribution towards less-prosperous citizens, while regressive taxes are to be avoided.
3. Horizontal equity among equivalent citizens	Are individuals or social groups in similar circumstances treated equivalently? If not, the tax may be adjudged to have an unfair incidence.
4. Fairness between Member States – GNI per capita	Especially in the EU, as an entity with limited cross-border solidarity, the ability to pay at the level of the Member State is a major consideration. Fairness between Member States could be based on proportionality or a more progressive regime.
5. Fairness between Member States – appropriability of revenue	A tax may be collected in one Member State, but the true tax-payer may not be a resident of that Member State because of accounting rules, tax exemptions or the location of head offices. Does tax collection at the Member State level fail to reflect the true incidence of the tax among members of the EU?
Administrative and political factors	Criteria that concern different facets of the administration and implementation of the revenue-raising system or are more overtly political in character
6. Sufficiency of revenue	Does the resource raise enough revenue to cover all, or a sizeable proportion of the total needed?
7. Stability as revenue source	Does the yield vary, for example over the economic cycle, in a way that risks a shortfall in aggregate revenue that then has to be found from alternative sources, or a surplus that will need to be redistributed?
8. Other administrative considerations	Any other issues, such as susceptibility to evasion, collection costs, need for revenue sharing between tiers of government and so on.
9. Link to EU policy concerns	How well does the proposed tax correspond to policy domains in which the EU is prominent? If there is an identifiable tax base that is positively affected by EU policies, there may be a stronger political rationale for an imposition on it.
10. Visibility and transparency to taxpayers	Will individual taxpayers be more aware that they are contributing to the EU when paying the tax, thereby rendering the tax more legitimate?
11. Autonomy for the EU level of government	Is the resource genuinely »owned« by the EU and where does the »power to tax« effectively lie? This criterion can be interpreted in two conflicting ways, because some argue that the EU level should not have such autonomy, others the contrary.

Source: Adapted from Begg, Enderlein, Le Cacheux and Mrak (2008).

taxes. It follows that the autonomy criterion may well exercise a veto on EU taxes or, if not, would need to be countered by a new political settlement in which the EU level acquired greater credibility as a fiscal authority. This would entail political development transcending the funding debate.

Fairness among Member States has long been a dominant criterion that manifests itself most obviously in the *juste retour* rhetoric that suffuses the politics of the EU budget. But for other actors, entirely different criteria are paramount. The European Parliament, for example, has repeatedly argued that visibility to citizens and greater

transparency ought to be given much greater priority. Thus the 2007 Lamassoure report asserts (paragraph 4) that:

the current system, with its four different resources and its several different rebate mechanisms, be they general ones in favour of one Member State such as the British rebate, or special ones such as rebates in financing other rebates, is excessively complex, lacks transparency and is completely incomprehensible to European citizens. It does nothing towards fulfilling the requirement of establishing a direct link between the Union and its citizens.

On a cautionary note, there is unlikely ever to be an ideal »tax for Europe« and the search for »the one« has been somewhat misguided, even misleading. Rather, it should be recognised that any credible source of revenue will be more attractive on some criteria than on others, but also that Member States (the prime decision-makers on own resources) and other stakeholders will have different preferences that will colour which instruments they are prepared to countenance. Differences in preferences would, in turn, determine the weight to be assigned to any particular criterion. For example, the sufficiency and stability of revenue is bound to be highly prominent for the European Commission which will not want to face uncertainty about its ability to finance planned expenditure.

Member States can be expected to be especially concerned about fairness among them, although they might also have conflicting opinions about how to calibrate fairness, with some championing the current proportional system, while others prefer a progressive system. Citizens are more likely to focus on the vertical and horizontal equity criteria, whereas governments are likely to consider these second-order criteria. In short, there is a strong normative dimension to selection of resources that is easily overlooked in the debate on whether or not EU taxes are justified.

2.2 A two-stage decision procedure

The Begg et al. (2008) study therefore advocated a two-stage methodology for choosing among resources. This approach would depart from the conventional one of identifying a potential instrument and then assessing its merits. Instead, it is proposed that the first stage should involve a political discussion about the characteristics that

a revenue source should exhibit. Such a discussion would culminate in a set of weights for the different criteria against which the various contenders would be judged. In a second stage, potential resources would be scored on the criteria and the weights applied to determine how much each criterion mattered in the overall assessment.

This can be illustrated by taking a limited set of criteria and giving them weights out of 100. Suppose weights of 40 each were assigned to fairness among Member States and revenue sufficiency, while 10 each are assigned to visibility and to connection with EU policies, how would the existing own resources fare if they were scored out of 10 on these four criteria? Table 2a illustrates this simple exercise. The TOR emerge poorly, not only because they obtain a low score on sufficiency and at best a middling one on the visibility and Member State fairness criteria, but also because the one criterion on which they score well because there is a clear link to trade, a prominent EU policy, is assigned only a low weight. By contrast, the GNI resource might score very poorly on the latter two criteria, but obtain a high overall score because of the heavy weight assigned to sufficiency and MS fairness, two criteria on which it scores favourably.

By the same token, altering the weighting scheme to place the emphasis on the European Parliament's preferences for visibility and on connecting revenue raising to EU policies reverses the attractions of the two resources. With this second weighting scheme, the high score for TOR on the fourth criterion, and the correspondingly low score for the GNI resource, tips the balance decisively against using the GNI resource (see Table 2b).

There are, inevitably, limits to the mechanical application of such a methodology, because the accuracy with which scores can be assigned is open to doubt and politics cannot easily be reduced to a formula. For instance, assigning a score of nine out of 10 to the GNI resource for inter-MS fairness could be challenged by those who believe that the current system of contributions proportional to GNI should be replaced by a more progressive system that takes proportionally more from richer counties. Equally, it would be possible to compare variants on the GNI resource if agreement could be reached on the principles for scoring, perhaps by assigning a higher score on inter-MS fairness to a mildly progressive GNI resource than to either a purely proportional one or a strongly progressive one. In other words, the method

Table 2a Illustrative weighting of criteria, favouring sufficiency and inter-member state fairness

	Criterion	Weight assigned	Score out of 10 (1=lowest)	Weighted score
Traditional own resources	Sufficiency	40	2	80
	Inter-MS fairness	40	5	200
	Visibility to citizens	10	5	50
	Link to EU policies	10	10	100
TOTAL				430/1000
GNI resource	Sufficiency	40	10	400
	Inter-MS fairness	40	9	360
	Visibility to citizens	10	3	30
	Link to EU policies	10	1	10
TOTAL				800/1000

Table 2b Illustrative weighting of criteria, favouring visibility and links to EU policies

	Criterion	Weight assigned	Score out of 10 (1=lowest)	Weighted score
Traditional own resources	Sufficiency	20	2	40
	Inter-MS fairness	10	5	50
	Visibility to citizens	40	5	200
	Link to EU policies	30	10	300
TOTAL				590/1000
GNI resource	Sufficiency	20	10	200
	Inter-MS fairness	10	9	90
	Visibility to citizens	40	3	120
	Link to EU policies	30	1	30
TOTAL				440/1000

can be made to work if a political procedure for agreeing the weighting and scoring systems can be devised: it is not that difficult.

The methodology can also, in principle, cope with criteria (such as autonomy for the EU level) where some actors regard »more« as a drawback rather than an advantage, by allowing for negative scores or weights, or by duplicating the criterion with one version favouring more autonomy and a second asserting the primacy of Member State competence in revenue raising. Again, purely mechanical application of the approach cannot produce a definitive answer, but its advantage is in forcing deci-

sion-makers to spell out what it is about different options that they find attractive or unappealing.

2.3 The budget review

In a communication on the EU Budget Review published on 19 October 2010, the European Commission (2010a) devotes one section to reforms of the financing side of the budget, and calls explicitly (as it has whenever long-term decisions on the budget are required) for an examination of the case for reform. The Commission notes (section 2.5) that:

From the beginning of the 1970s, the EU collected own resources deriving from common policies like the common customs tariff duties. The autonomy of these own resources has been gradually undermined and the current system of EU financing has evolved piecemeal into a confusing and opaque mix of contributions from national budgets, corrections and rebates. The connection between the original own resources and common EU policies has been lost, making the system less transparent and increasing doubts about fairness.

All this is true and the Commission goes on, in section 7 of the review, to discuss criteria for selecting alternative resources and to list a series of possible funding instruments. However, the communication does not signal any preferences and – rather lamely – says only that each of »these financing means has its particular characteristics and presents advantages and disadvantages«, promising to submit proposals at a later stage. The Commission list of potential revenue sources comprises many of the »usual suspects« – such as an EU VAT or corporate income tax – identified in a variety of previous studies or in previous Commission proposals and European Parliament resolutions (Lamassoure, 2007, gives a Parliament view). But where it has caught the attention of some governments and stakeholders is in putting »EU taxation of the financial sector« at the top of the list. It also lists three variants on energy/carbon taxes:

- (i) Revenue from the auction of greenhouse gas emissions trading permits
- (ii) A levy on air transport
- (iii) An EU energy tax

3. Plausible options for new resources

Many different options for revenue streams to fund the EU budget have been canvassed over the years, several of which recur repeatedly (Begg et al., 2008, provides an overview). Favourites include a share of VAT receipts, different forms of energy or carbon taxes and corporate income tax, so that the Commission communication is in many ways in the mainstream of the literature. Its espousal of taxation of the financial sector is an innovation. This section looks in more depth at a selection of possible EU taxes, but starts by examining some more general issues.

3.1 General considerations

Any of the options suggested in the communication could, in principle, become EU resources, so long as there was the political will to implement them. All would pose technical challenges, but none of these would be insuperable and (as discussed in Begg et al., 2008) there are further options – such as using central bank monetary income, other consumption taxes or personal income tax – that could be considered. A crucial starting assumption for any change is that the revenue requirement would not change, so that one euro raised from a new resource would allow the call on the current GNI resource to fall by one euro. This principle of revenue neutrality is vital because of the ease with which the media and unscrupulous political opponents can present any change as an increase in taxation, rather than a substitution of an existing resource by a new one.

An unavoidable difficulty in introducing a new resource (or, conceivably, multiple resources) capable of raising all, or a substantial proportion of, the EU's financing is that its yield will not be perfectly predictable. Consequently, some means of ensuring that the EU budget is balanced would be needed. If the new resource cannot realistically raise enough revenue, there will be a continuing need for a complementary resource to top up the income. If it raises too much, some means of distributing the surplus will be needed. In practice, a GNI resource modelled on the current one is likely to be the answer, albeit on a much diminished scale, because of its invaluable property of acting as the residual element. A shortfall would be met by calls for national contributions, but there is no great difficulty in designing the resource symmetrically such that a surplus would be distributed back to Member States using the same key.

A further issue is whether an EU tax should have ambitions other than revenue raising. Environmental taxes, in particular, are often justified on the grounds that they deter socially damaging behaviour. Such taxes, often labelled »Pigouvian« after the eminent economist who first analysed them, are able to generate a double dividend of engendering a welfare-enhancing distortion of economic activity (for example, by penalising excessive use of coal or hydrocarbons, thereby lowering carbon emissions) at the same time as generating revenue. In the EU context, further benefits could stem from the demon-

stration of the EU doing what citizens wanted, potentially creating a triple dividend.

But assigning multiple goals to a single policy instrument can be tricky. If a tax is highly successful in altering behaviour, it erodes the tax base and could see attrition of the revenue. Conversely, relying on it to raise money can undermine the incentives to deal with the adverse effects. In addition, competing political imperatives could lead to uncomfortable compromises about how to set the tax. Thus, to protect revenue, the tax should be set at the level that produces the highest yield, but if the objective is deterrence, the rate should be set to achieve a desired level of change in behaviour, such as a target for lowering emissions. For something as sensitive as the EU budget, the revenue considerations would have to come first.

3.2 Carbon or energy taxes

Dealing with the threats of climate change is one of what are becoming known as the grand challenges facing the EU, and there is manifestly growing alarm in Europe about energy security, given the political volatility that characterises many of the oil and gas producing countries. For these reasons, fostering change in patterns of energy use in Europe is already a political and policy priority. Consequently, a strong connection can be made between a core EU policy and carbon or energy taxes. Insofar as any tax can be popular, there is likely to be support for such taxes, and the likelihood is that they would be visible to citizens. On political criteria, therefore, they ought to fare well.

Although much will depend on the detail, there are many potential economic and administrative hurdles to overcome if energy taxes are to be viable as EU taxes. Environmental taxes raise at least two per cent of GDP in the Member States (the majority generally coming from energy taxes, especially motor vehicle fuel duties), with some reaching five per cent, so that there is certainly scope for raising enough revenue. However, the nature of national policies differs and would be quite hard to harmonise. There are also concerns that the unilateral imposition of energy taxes in Europe, but not in the rest of the world, would be detrimental to European competitiveness. Carbon taxes or emissions trading charges imposed on producers are especially vulnerable in this respect.

Whether energy taxes would be fair is not easy to answer without a precise definition of the proposed tax, but some general propositions can be identified. Certain energy taxes penalise citizens who have unavoidable energy demands: in rural areas, for example, there may be few (if any) alternatives to the use of the private car for meeting basic needs, so that a tax on fuel would fall more heavily on citizens in rural areas than urban areas. Those in cold, hot or humid climates, tend to have greater needs for space heating or cooling than those in temperate areas and would be penalised for higher direct or indirect carbon emissions, and so on.

Another concern about energy or carbon taxes is that there could be conflict between their role in deterring energy use and their reliability in funding the EU budget. That said, there are forms of such taxes that would fall mainly on consumers and would still be robust in revenue raising. Both motor vehicle fuel taxes and a possible levy on air transport are good examples of revenue sources that have bases likely to be price inelastic – that is, where the underlying activity would not diminish markedly if the imposition of a tax raised the price. Indeed, in both cases, the more likely outcome of a tax-induced price increase is that the growth of what have long been buoyant markets would simply slow down, rather than leading to a decline in sales; this would ensure stable revenue.

3.2.1 Examples of energy taxes

An air transport levy has been advocated recently in a variety of contexts, including as a means of generating revenue for development aid, but also to slow the growth of a polluting activity. Most forecasts suggest that air travel is set to continue its growth across the EU, even if fuel prices continue to rise. Moreover, many commentators consider the air transport sector to be under-taxed, partly as a result of decades-old international conventions that exclude taxation of aviation fuel. Several countries have introduced passenger »levies« (an artful term used to circumvent the international agreements), a good example being the recently revised UK one. Germany, too, has just introduced a flights tax very similar to the UK one, although other countries which had them have either abandoned the idea or lowered the rate under pressure from the travel and tourist industries. Box 2 presents the main features of the UK levy.

Box 2 The UK air passenger duty

A levy on passengers – the air passenger duty (APD) – was introduced in the UK in the Finance Act of 1994 and has been subject to various amendments since then. For commercial flights, each passenger is charged a flat rate for departure from a UK airport. There is now a lower charge on those travelling on low-cost services, but a higher rate was imposed on business and first class passengers and those travelling outside the European Economic Area, with bands depending on distance. According to Treasury projections published in the UK budget presented in June 2010, APD is expected to raise about £2.9 billion (just under 0.2 per cent of nominal GDP) in the 2011/12 fiscal year in which the rate increases introduced in November 2010 will have been in force for a full year.

In 2007, it was announced (though never implemented) that the per-passenger duty would be replaced by a per-flight charge, a change justified on the grounds that it is the flight that creates environmental damage, with the number of passengers on board making only a marginal difference to the emission of pollutants.⁴ If it were extended to freight flights it would raise additional revenue. The 2010 government coalition agreement promises to replace the APD with a per-flight duty, thereby fulfilling what the previous government had already proposed, but in the coalition's June 2010 budget, no change was effected and it remains under review.

If an air travel levy were extended Europe-wide, it could potentially generate only a proportion of the EU's revenue needs, but it should be stable revenue and might be part of an own resources reform that could be implemented quickly to lower the share of national contributions. An APD will work best if imposed multilaterally or at EU level, because the scope for avoidance by the air transport industry would be diminished, whereas if imposed unilaterally there is some risk – typically, it has to be said, exaggerated by the interests affected – that airlines will relocate to airports in countries where there is no such imposition. There are differences in the extent to which residents of different countries use air travel, which imply some problems with horizontal equity, but the structure of the UK and German mechanisms goes some way towards vertical equity by charging more to those buying more expensive tickets (whether because of class of travel or destination). Another possible drawback is that by targeting a single industry it would be distortionary, a point emphasised in tourist industry objections, although as with other »Pigouvian« taxes this could be justified on the grounds that polluters should pay. For most Member States, such a duty would be a new tax that might provoke political objections, but precisely by being new, it could achieve political visibility for the EU level and chime with a key policy objective.

Every EU Member State already has motor vehicle fuel taxes, but there are differences in the rates, both between countries and between particular fuels (diesel, petrol, LPG). However, achieving harmonisation would not be that great a technical challenge, although the spirited defence of higher carbon emission targets by the German government, following representations by their car manufacturers, points to one area of political sensitivity. Vertical and horizontal equity would not be respected, as patterns of car use vary considerably, but on many of the criteria put forward above, a motor vehicle fuel tax would be viable as an EU tax. A potential difficulty would be in establishing rules for business use of these hydrocarbons, including provisions to limit the scope for tax avoidance. Other practicalities to confront would be how to apportion the revenue among levels of government, including whether there ought to be a base rate as an EU tax, with the revenue accruing directly to the EU level, and a supplementary rate set by the Member State which retains the proceeds.

4. The case for the change was set out in detail in a government consultation – HM Treasury and HMRC (2008).

3.3 The case for corporate taxation

Using a corporate income tax (CIT) to fund the EU budget has a number of attractions. The single market is a fundamental aim of the European Union and has been pivotal in creating market opportunities across national borders. The profits of many companies, especially the largest ones, derive from activity in several, if not all, Member States (and other parts of the world), so that there is a case for taxing these profits at EU level, rather than in the individual Member State which happens to be its headquarters. Doing so would reduce the inequity of inter-Member State appropriation of the yield from the tax and would also be economically efficient to the extent that it would deter companies from selecting a location just for tax reasons.

The fact that CIT is levied in all Member States means that systems are already in place to collect the tax. Although the yields of these national taxes fluctuate substantially over the economic cycle, they typically account for well over two per cent of GDP, so that they would be more than sufficient to cover the EU budget at around its present level in its entirety. Consequently, there is no great conceptual difficulty in envisaging CIT becoming a major revenue source for the EU, as it would essentially be a matter of re-assigning its revenue from the national level – or in some Member States, the sub-national level or a combination of national and sub-national – to the EU's coffers.

The main drawbacks of CIT are both technical and political. In the former category, the biggest stumbling-block is that there simply is not a common tax base, because the Member States all have their own approaches to exemptions, accounting rules and so on. Establishing a common consolidated corporate tax base (CCCTB) has been on the agenda of the EU for many years and would, moreover, constitute an important step towards enhancing the single market. However, it has proved to be a thorny issue and does not look like being settled soon. In the absence of a CCCTB, there would inevitably be differences in the incidence of the tax on companies with similar levels of profitability, so that horizontal equity would not be respected.

Political objections derive from the fact that corporate taxation is an instrument that many governments use to shape their economies. For example, allowances for R&D

investment are common, but the range of such allowances will typically be customised to the industrial structure of the Member State. Low or flat taxes have been used by certain Member States to attract inward investment and those that have such CIT arrangements would be reluctant to forgo so potent an economic development policy, although other Member States that feel they are denied revenue for the mirror-image reason might be more enthusiastic.

Introducing CIT as an EU tax would also require procedures for dealing with fluctuations in the yield of the tax over the economic cycle, over-shooting of the revenue and, conceivably, periods when the yield in a particular Member State rises or falls for exceptional reasons. Suppose, for example, that the tax always raised more than the revenue required for the EU budget. Should the surplus be distributed to the Member States and, if so, using what »key« (GDP being the most obvious one), or should it be retained by the EU level, perhaps enabling it to build up its financial surplus?

All these considerations suggest that CIT would be a strong candidate on some of the criteria set out above, so that it has the potential to be a good EU revenue source. But it would also attract negative ratings on a number of other criteria, and would thus require solutions for several thorny problems to be viable. Given the likely political resistance to change, such solutions would take time to negotiate. Consequently, although CIT has attributes that are alluring as an EU tax, it is not an option that could plausibly be implemented soon. However, if there is the political will to confront the obstacles, its attractions could make it more plausible in the longer term – notwithstanding Keynes's well-known dictum.⁵

3.4 The scope for increased taxation of the financial sector

Financial companies are often portrayed as serial tax-avoiders and as contributing too little to the revenue needs of the state. While it is undoubtedly true that many in finance go to great lengths to reduce their tax liabilities, it is simply wrong to assert that the sector does not contribute substantially to the public coffers. Indeed, one

5. »The long run is a misleading guide to current affairs. In the long run we are all dead.« John Maynard Keynes, *A Tract on Monetary Reform*, Chapter 3 (1923).

of the causes of the structural budget deficits that have surfaced in many Member States since the start of the crisis in 2008 is that governments had become *too* dependent on revenues from the financial sector, based on the exceptional profits associated with bubbles and high levels of speculative activity, not to mention huge bonuses. According to the Commission (2010b), the financial sector raised about 20 per cent of corporate income tax in the years before the crisis.

The idea of a »Tobin« tax on financial transactions has been around for many years. It was originally proposed to curb excessive trading on financial markets and the resulting volatility, with its destabilising consequences. As James Tobin himself put it, the idea was to throw sand in the wheels of a financial system that was spinning far too rapidly. Subsequently, many campaigners have advocated a financial transactions tax (FTT) to fund development assistance for poor countries, on the grounds that as the financial sector was a major beneficiary of globalisation it should be asked to contribute to the welfare of those who have lost out from the opening up of global markets. In the wake of the financial crisis of 2008/9, a new rationale has emerged in which the case for taxing the financial sector is to repay the tax-payer for rescuing the banks and insurers.

A compelling political case for an FTT (or some other form of taxation of the sector) has therefore been built up in recent years, and there has been widespread and high-level political support for the introduction of such taxes, including at successive G20 meetings. Recently, several studies have also attempted to assess the viability of different approaches and the practicalities of introducing different options. The IMF (2010), for example, has studied the case for a financial activity tax (FAT) designed to extract revenue based on the added value of the sector, while a number of others have concentrated on the FTT.

The gist of these studies is that, at a relatively low level, an FTT could generate a sizeable flow of revenue, and that many of the presumed obstacles – notably the fear that such a levy would easily be avoided by financial market actors – can be overcome. Moreover, the increased sophistication and centralisation of settlement systems has meant that the mechanics of collecting the tax have become easier. Estimates are subject to considerable uncertainty, but they suggest that taxing cur-

rency transactions at a rate of 0.005 (one two-hundredth of a percentage point, or roughly 10 per cent of the typical transaction cost) could yield around 20–40 billion euros worldwide, much of it from European financial centres. Spreading the net to other heavily traded financial instruments could multiply the yield, with some estimates reaching as high as 350 billion euros if over-the-counter transactions are included, as well as those in exchanges. The latter figure seems implausibly high since it would be of the order of one per cent of global GDP levied on a sector that, globally, accounts for around five per cent of GDP (depending on how it is defined), most of it consisting of the more routine provision of banking and insurance services, not the speculative activity which is usually associated with an FTT.

The uncertainties on yield are of various sorts. First, a tax may simply deter the activity to such an extent that the tax base shrinks markedly. Second, the undoubted creativity of financial markets may result in substitution of the taxed instrument by one that is not liable to pay; and third, the trade may shift to a market in a jurisdiction not subject to the tax. All of these phenomena are discussed in the literature and acknowledged to be risks, but not terminal ones.

However, to be a viable means of financing the EU budget, an FTT would face various hurdles, not least because it is hard to determine where the true incidence of the tax falls and how reliable it would be as a revenue stream. An IDS policy briefing note written by McCulloch and Pacillo (2010) argues that although the financial intermediaries at the heart of the markets would bear the initial costs, the true incidence will ultimately be on consumers, although they nevertheless believe that an FTT would weigh more heavily on the better-off than possible alternatives, such as VAT on financial services, and thus be progressive. There would certainly be a major struggle in Europe to define the tax base and the fact that London is the pre-eminent financial centre in Europe, resulting in a high proportion of the potential revenue accruing in the first instance to the UK, would be bound to lead to claims from London that this is »our« money.⁶

6. It is worth noting that essentially the same dispute arises over the collection of the traditional own resources. The per capita amounts collected by the Dutch and the Belgians far exceed those of the Austrians and the Germans, two neighbouring countries with similar levels of per capita consumer expenditure. The explanation is simple: Dutch and Belgian ports are the points of entry for extra-EU imports at which customs duties are levied, even though the final consumer may be further up the Rhine. Not surprisingly, the Dutch argue that the revenue collected should be counted as part of their gross contribution to the EU, while their neighbours think otherwise.

Within the EU, the financial sector, according to data derived from Eurostat statistics presented in a Commission document (2010b), accounted for around 5.3 per cent of EU total value added (effectively, GDP) in 2008, but its share ranged from just 2.8 per cent in Finland and 3.4 per cent in Germany and Slovakia to 9.6 per cent in the UK, 10.3 per cent in Ireland and a staggering 28.9 per cent in Luxembourg.⁷ However, the more specialised trading activities that are usually envisaged as the subject of an FTT are highly concentrated in London. Using a wide definition (FTT1) that includes derivatives, Schulmeister et al. (2008) estimate that for a sample of seven EU Member States, 71.3 per cent of the revenue would accrue in the UK, 15.5 per cent in Germany, 6.6 per cent in France and just 2.2 per cent in Italy. A narrower definition (FTT2) that only covers share and bond trading would still see 36 per cent of the tax raised from the London Stock Exchange and 25 per cent from the Spanish BME,⁸ compared to 14.6 per cent from Frankfurt and much smaller amounts from other trading platforms.

3.5 Options compared

The sheer political sensitivity of picking any EU funding instrument, be it the current mix of resources or any new ones, means that there will always be profound disagreements not just about the options themselves, but also about their strengths and weaknesses. How to appraise some of the attributes will, moreover, depend on precisely how the EU tax is configured and this design aspect is another factor to take into account in choosing.

To provoke debate, more than to give definitive answers, the tables overleaf provide overviews of the viability of, first, a generic carbon tax, then of four specific potential EU funding resources. Each is tentatively assessed on the eleven criteria, although it should be stressed that these assessments themselves are open to challenge, as there is inevitably a subjective element for some of them – notably those that necessitate a political rather than a factual interpretation. Readers are therefore invited to

7. Data from the Bank for International Settlements quoted in the same paper suggest that the financial sector accounts for a somewhat higher proportion of EU and euro area value added, at 5.8 per cent in 2008, while the comparable figure for the US is around eight per cent. These differences highlight the difficulties inherent in measuring its value added.

8. The high Spanish figure arises because of a very high level of bond trading, as reported by the Commission (2010b). The estimated yield is derived from a uniform levy on all transactions, irrespective of value, and should be interpreted with caution.

ponder how they would assess each contender on the various criteria. The tables distinguish between criteria that are strengths and weaknesses of the potential resource, but also draw attention to those for which the verdict is likely to depend on how the resource is designed.

4. Conclusions

The debate on whether or not the EU budget should be financed by an EU tax is a curious one. It is bedevilled by disinformation, prejudice and arguments that are frequently specious or exaggerated, but it is really a political contest about who should possess the power to tax. Member States, not surprisingly, defend this power doggedly and would see any concession that gave the European Parliament more say as the thin end of an uncomfortable wedge. But an evident irony is that the Parliament today can influence spending commitments without having to take the hard decisions about taxes: what some have called – inverting the original logic of the Boston Tea Party – »representation without taxation«. In addition, the fact that any new EU tax would allow a reduction in national contributions is routinely forgotten, and many of the rational arguments for and against are prone to be overshadowed. It is, therefore, important to distinguish between the technical and economic arguments for having an EU tax, on the one hand, and the political advantages or drawbacks, on the other, recognising that in the EU of today, the latter will be paramount.

As a technical proposition, there is no over-arching obstacle to an EU tax (or taxes) and there are plenty of options that could be viable, although some complications would have to be expected in harmonising tax bases and establishing the necessary administrative structures. Equally, there is unlikely ever to be a contender that is the »ideal« EU tax, because any conceivable instrument will have attributes that someone will, with good reason, oppose. Taxes or levies linked to carbon emissions, corporate income or financial activity are credible, but would have markedly different properties as EU resources. For this reason, this paper advocates an approach to selecting resources that first settles what properties a good resource should possess and then focuses on how well the different options fit the preferred criteria.

Table 3a: Overview of viability as EU resource: a carbon tax (generic)

Assessment on eleven criteria			Comment
Advantages	Dependent on design	Drawbacks	
<ul style="list-style-type: none"> - Link to EU policy - Revenue stability - Autonomy for EU - Visibility 	<ul style="list-style-type: none"> - Horizontal equity - Vertical equity - Revenue sufficiency - MS appropriability 	<ul style="list-style-type: none"> - Inter-MS fairness - Economic efficiency - Other administrative 	Tax could be either on consumers or producers of carbon
Overall verdict	Chance of being accepted	Reason for possible veto	
	Low to moderate	Big differences in carbon dependence among MS Risks to competitiveness in global markets	

Table 3b: Overview of viability as EU resource: air passenger duty as a form of carbon tax

Assessment on eleven criteria			Comment
Advantages	Dependent on design	Drawbacks	
<ul style="list-style-type: none"> - Link to EU policy - Revenue stability - Autonomy for EU - Visibility - Vertical equity 	<ul style="list-style-type: none"> - Horizontal equity - Other administrative - Economic efficiency - MS appropriability 	<ul style="list-style-type: none"> - Inter-MS fairness - Revenue sufficiency 	Easy to collect and there are existing models Could only raise a fraction of revenue needed
Overall verdict	Chance of being accepted	Reason for possible veto	
	Moderate Could be introduced fairly soon	Would raise too small a proportion of EU revenue International obligations on not taxing air transport	

Table 3c: Overview of viability as EU resource: motor vehicle fuel tax as a form of carbon tax

Assessment on eleven criteria			Comment
Advantages	Dependent on design	Drawbacks	
<ul style="list-style-type: none"> - Revenue stability - Revenue sufficiency - MS appropriability - Link to EU policy 	<ul style="list-style-type: none"> - Economic efficiency - Other administrative - Vertical equity - Visibility 	<ul style="list-style-type: none"> - Horizontal equity - Autonomy for EU - Inter-MS fairness 	Easy to collect and already available, but problems of apportioning any surplus revenue Might need rethinking of tax incidence and impact
Overall verdict	Chance of being accepted	Reason for possible veto	
	Moderate Could be introduced fairly soon	An important national tax already, but risk of adding to business costs	

Table 3d: Overview of viability as EU resource: corporate income tax

Assessment on eleven criteria			Comment
Advantages	Dependent on design	Drawbacks	
<ul style="list-style-type: none"> – Link to EU policy – Revenue sufficiency – MS appropriability – Horizontal equity 	<ul style="list-style-type: none"> – Visibility – Vertical equity – Inter-MS fairness – Economic efficiency 	<ul style="list-style-type: none"> – Revenue stability – Autonomy for EU – Other administrative 	Would need prior definition of tax base and some basis for sharing of income if yield exceeds revenue needs
Overall verdict	Chance of being accepted	Reason for possible veto	
	Low to moderate in the short-term, more credible longer-term	Political and social sensitivity for several MSs Worries about loss of autonomy	

Table 3e: Overview of viability as EU resource: financial transactions tax

Assessment on eleven criteria			Comment
Advantages	Dependent on design	Drawbacks	
<ul style="list-style-type: none"> – Link to EU policy – Horizontal equity – Vertical equity – Visibility 	<ul style="list-style-type: none"> – Autonomy for EU – Revenue sufficiency – MS appropriability 	<ul style="list-style-type: none"> – Revenue stability – Economic efficiency – Inter-MS fairness – Other administrative 	Would need to be established as a new tax Taxing transactions as opposed to added value not efficient
Overall verdict	Chance of being accepted	Reason for possible veto	
	Low to moderate, but may be too closely linked to post-crisis thinking	Impact on certain MS Risks of avoidance	

A suitable resource clearly has to be durable because, once adopted, it is likely to be in place for decades: the traditional own resources, after all, will have been in use for over forty years by the time a new budget deal is agreed for the period after 2013. It follows that it would be a mistake to base a decision on short-term considerations. For example, a financial transactions tax has a particular appeal today in the aftermath of the financial crisis and would capitalise on current anti-banker sentiment, but will also have to make sense 10 years from now.

4.1 Making a choice of EU resource

Returning to the argumentation of section 2.2, any choice of EU resource will depend on what attributes decision-makers want to favour in such a resource, so that it is instructive to compare the options. Any comparison of the four potential EU taxes discussed in section

3.5 – plainly, a far from exhaustive selection – also has to be benchmarked against the current system. EU autonomy (and its corollary of Member State control of key revenue streams) is often at the heart of the debate and most Member States remain very keen to protect this power, a perspective that would immediately end any discussion of an EU tax. But autonomy can also be interpreted more narrowly as whether a proposed EU tax is one that would infringe on a key national economic policy instrument, CIT being an example (others, with social aims, might include excise duties on alcohol and tobacco). Some other potential resources may not be subject to the same sensitivities, perhaps more so if they are new revenue sources.

The great strengths of the current system, with the dominant role of national contributions, are in ensuring that the EU level is reliably funded and that the burden among Member States is fair. It follows that, if these are

the most important criteria, the case for change will be very hard to make. However, some critics assert that although charging each Member State the same proportion of its GNI is tolerably fair (and could, if desired, also be rendered more progressive by charging a higher rate to richer Member States), the proliferation of correction mechanisms weakens the argument. Indeed, after corrections, the proportion of GNI paid by some of the better-off Member States is markedly lower than those charged to the poorest, flouting the ability-to-pay principle. In addition, the current system falls down on the horizontal and vertical equity criteria, because what an individual citizen pays is determined by the national tax mix, so that two citizens of identical means in different Member States could face a very different aggregate tax burden and thus contribute unevenly to funding EU spending.

If a close link to EU policies is a desired attribute of a future EU resource, any of the prospective new options discussed in section 3.5 would be an improvement over current arrangements. Achieving visibility would conceivably be enhanced most by a new tax such as FTT or possibly the APD, both of which would also be reasonably positive on vertical equity, though less so on horizontal equity. But neither would be able to raise enough money to fund all of the EU budget, in contrast to both a motor vehicle fuel tax and the CIT. However, the latter two would intrude far more into areas where Member States want the tax to be part of domestic economic and social policy.

4.2 Political feasibility

A change from the present system is bound to involve some shifts in net fiscal burdens, because however carefully a new resource is constructed, there are bound to be winners and losers, whether among citizens or Member States, and it is inevitable that the losers will make more noise than the winners. New resources will also require some recalibration of existing arrangements, such as to achieve budget balance, which (given that a change to the Treaty to remove the EU's obligation to balance the budget is unlikely) would require some balancing mechanism. This would probably have to be a GNI-related resource that either topped up or paid back, depending on whether the yield of any new tax fell short of or exceeded the EU's revenue requirement.

For these and other reasons, the introduction of an EU tax is likely to be a messy exercise. It may therefore make sense to proceed by stages, perhaps by bringing in a new tax to substitute for part of the GNI resource in the short-term – say for the next multi-annual budget deal – then extending an EU tax subsequently. If this is the aim, the low yield of a resource such as FTT or APD would be an attraction rather than a problem, contributing around 20–30 per cent of the revenue requirement. A longer time-frame would also afford scope to iron out administrative complications surrounding higher yield taxes such as CIT or motor vehicles fuel tax and to configure them so as to enhance their attractiveness as EU resources.

Selling an EU tax to a sceptical public will not be simple. It will not offer easy solutions to the intractable problems of net balances and the resulting corrections, but it might help to lessen the acrimony surrounding the issue. Nor will a switch from national contributions to an EU tax have much impact on the big economic governance questions currently dominating policy debates. In time, some more flexibility in EU finances might be part of an answer to future sovereign debt problems, but the EU needs first to decide what degree and form of fiscal union it is prepared to countenance. But a dispassionate analysis also shows that governments do not have that much to fear from turning to a new tax to fund at least part of the EU's expenditure.

Some heads of government seem to be mellowing: witness a speech by George Papandreou at the French Finance Ministry on 6 January 2011 in which he specifically mentioned FTT and a CO₂ tax as innovative financial tools. Others, plainly, remain intransigent, but in a period when bailouts have become tolerable and a whole new economic governance architecture is being constructed, what was once *parfaitement inopportune* could suddenly make sense.

Will the EU's leaders be prepared to take the plunge?



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