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Peter Zangl*

The Financing of the Community after the Edinburgh European Council

At its Edinburgh meeting on 11th and 12th December 1992 the European Council came to a number of conclusions regarding the future financing of the Community. The following article examines the implications of the new financial perspective.

The signing in Maastricht of the Treaty on European Union on 7 February 1992 ushered in a new era for the Community. The new definition of powers in Article 3 and the enshrinement of the subsidiarity principle in Article 3b have financial implications which need to be examined.

The Commission began this on 11 February 1992 in its communication to the Council and Parliament entitled "From the Single European Act to Maastricht and Beyond" (COM(92) 2000), better known as the "Delors II package". Lengthy negotiations on the proposals followed. Parliament expressed its views in a resolution on 16. 6. 1992¹ leading to the conclusions of the Edinburgh Council on 12 December 1992.

Lessons of the 1988 Financial Reform

The proposals in the "Delors II package" arise naturally out of the 1988 reforms and the "Delors I package". At the time, the aim was to secure the Community's financing after years of crisis and to provide financial support for the implementation of the Single European Act and the completion of the Single Market. The first priority was to ensure that the Community could rely on having sufficient resources with each Member State paying its fair share. On the expenditure side, budgetary discipline arrangements were introduced to make sure the additional resources were used for their intended purpose and not to fund other purposes, for instance, the EAGGF Guarantee Section.

The regulatory framework was provided by the 1988

decision on agricultural budgetary discipline: observance of the agricultural guideline; monthly monitoring of expenditure (early warning system); and the introduction of stabilizers. The Interinstitutional Agreement and the financial perspective committed Parliament, the Council and the Commission to respect these principles, particularly the ceilings on the six categories of expenditure, and effectively held the financial reform together. The annual nature of the budget was reinforced and led to a remodelling of the Financial Regulation.

The agreement, which was for 1988-1992 only, proved instrumental in achieving all the principal objectives, although it has to be said that external factors, such as the ECU/US\$ parity and the size of world crops, also played a part.

- Peace reigned on the budgetary front throughout the period, each budget being adopted relatively painlessly before the beginning of the financial year.
- Agricultural expenditure was held below the agricultural guideline throughout the period.
- Economic and social cohesion expenditure – the doubling of the structural Funds – conformed to the decisions taken in 1988.
- Supporting policies for the single market were properly funded.

In addition, economic growth was such that the Community was able to stay under the own resources ceiling decided in 1988 by a sufficient margin to finance its

* Commission of the European Communities. This text contains the personal opinions of the author and does not necessarily represent those of the Commission of the European Communities.

¹ In relation to Parliament's approach, see also: G. Stahl: Die Europäische Gemeinschaft vor einer erneuten Finanzkrise?, in: Wirtschaftsdienst, No. 11, 1992, pp. 80-84.

Table 1
Past Financial Perspective
and 1997 Proposal by the Commission
 (ECU million – 1992 prices)

Commitment appropriations	1987	1992	1997
I. Common agricultural policy	32.7	35.3	39.6
II. Structural measures (including Cohesion Fund)	9.1	18.6	29.3
III. Internal policies (other than structural measures)	1.9	4	6.9
IV. External action	1.4	3.6	6.3
V. Administrative expenditure (and repayments)		5.9	4.4
VI. Reserves	0	1	1.4
Total	51	66.5	87.5
Payment appropriations required – as a percentage of GNP	49.4 1.05%	63.2 1.15%	83.2 1.34%
Own resources ceiling (% GNP)	(no ceiling) (except VAT limited at 1.40% call rate)	1.20%	1.37%

growing external commitments – in Central and Eastern Europe in particular.

On the debit side, attempts to bring Community financing closer into line with Member States' ability to pay proved disappointing as the yield from the GNP-based fourth resource was lower than expected.

Against this generally favourable background, the Commission put forward a second financial package for 1993-1997 centred around three main themes:²

- continued strict budgetary discipline, as far as possible on the basis of an interinstitutional agreement and the financial perspective;
- proper funding of Community activities under the Maastricht Treaty;
- a financing structure more consistent with each Member State's ability to contribute.

The Community's Financial Requirements

The estimate of Community requirements allowed, in conformity with the subsidiarity principle, for the funding of ongoing policies and the implementation of the Maastricht decisions (see Table 1). Three priorities were established:

- external action;
- economic and social cohesion;
- enhanced economic competitiveness.

In the Commission's view, to properly fund the new objectives and continue along the path of Community integration, an additional ECU 21 billion would be needed between 1992 and 1997, including:

- ECU 2.7 billion for the reformed CAP;
- ECU 11 billion for economic and social cohesion (a prerequisite for putting Maastricht into practice);
- ECU 3 billion for internal policies;
- ECU 3 billion for external action.

These amounts are for achieving the following objectives:

Resources need to be made available for implementing Common Agricultural Policy (CAP) reform measures. After the 1988 financial reorganization, this fundamental reform will lead to the gradual replacement of price guarantees by direct aids. Under the new CAP, expenditure will fluctuate less and estimates of requirements will be more reliable. However, there will be a transition period during which expenditure may at times be difficult to control. In any event, without the reform, there would in the medium term have been a much bigger increase in agricultural expenditure than looks likely now.

With regard to *economic and social cohesion*, the Maastricht Treaty provides for a review of the operation and effectiveness of structural Fund intervention. In addition, resources have to be found for the Cohesion Fund so that Community expenditure on cohesion in the recipient countries can be increased to twice the amount spent on their Objective 1 regions in 1992.

Besides training and recycling measures for workers faced with job changes, the Commission took the view that much more research is needed if *competitiveness* is to improve, as well as strong Community support for trans-European networks; however, not all these networks should receive financing, which is best restricted to a small number of projects of uncertain microeconomic profitability but of crucial importance to the operation and effectiveness of the network as a whole. In addition to these measures specifically designed to strengthen the competitiveness of European economies, funding for internal action should ensure the continuation of ongoing Community measures and particularly those essential to the efficient operation of the single market.

If the Community is to win itself a bigger role on the

² For a more detailed analysis, see e. g.: C. Groutage, P. Zangl: Next steps in EC Budgetary policy, in: H. Cowie (ed.): Towards Fiscal Federalism, Federal Trust for Education and Research, London 1992, pp. 1-9.

world stage, it will need to spend more money. This is not just a matter of multiplying measures in favour of Central and Eastern Europe; measures will also have to be taken in the Mediterranean basin and in Asia, Latin America and Africa. An increased Community presence in these areas will help strengthen their economies and promote democracy and peace.³

Greater Fairness in Financing the Budget

The Community's over-dependence on VAT has not significantly decreased since 1988. As a result, the allocation of Member States' contributions is still far from equitable. Taking GNP as a measure of ability to pay, in the four countries with a per capita GNP (in purchasing power parities terms) below 90% of the Community average, the VAT base exceeds 55% of their GNP compared with a Community average of 51%. Since 55% of the Community budget comes from VAT, the least prosperous Member States end up paying more than is warranted by their share of the Community's GNP. There are two ways of correcting this:

- putting a ceiling on the proportion of GNP which may be accounted for by the VAT base in each Member State (capping);
- reducing VAT's share in the financing of the budget.

Both these aspects already had their place in the 1988 reform which restricted the VAT bases to 55% of GNP and created a fourth resource proportional to GNP (instead of increasing the VAT call-in rate).

Although some progress was indeed made, these adjustments did not fully achieve their objective; the Commission therefore proposed capping VAT further (at 50% of GNP) and reducing the call-in rate from 1.4% to 1%, the ultimate aim being to reduce VAT's share in the financing of the Community budget from 55% to 35%.

Budgetary Discipline

The encouraging results obtained since 1988 persuaded the Commission to propose that budgetary discipline be continued and some necessary improvements be made. The proposals were:

- sign a new Interinstitutional Agreement containing a financial perspective;⁴
- retain the budgetary discipline arrangements in an adjusted version;

- pursue the principles of budget annuality and cost-effectiveness.

The fact that there was an Interinstitutional Agreement and that by and large it worked satisfactorily meant that the new budgetary discipline agreed in 1988 could be implemented against a background of reasonably orderly relations between the three institutions concerned with the result that there was peace on the budgetary front throughout the lifetime of the Agreement. The Commission therefore proposed that it be renewed, in a slightly more flexible format to avoid the many cumbersome revision procedures that had characterized the previous period; this flexibility, however, should not relax the binding expenditure ceilings for each of the categories in the financial perspective.

Achieving budgetary discipline is easier if expenditure is strictly defined within a financial perspective contractually agreed by all three institutions. The de facto co-responsibility arising from such an agreement tightens discipline further since compulsory expenditure cannot overrun to the detriment of non-compulsory expenditure and vice-versa. There is no question that it was much easier to respect the agricultural guideline, even when it appeared under threat, knowing that it could not be exceeded or increased without Parliament's assent.

Finally, each of the annual budgets was adopted in time for execution to begin on 1 January; this has considerably strengthened the principle of annuality and thus the principle of cost-effectiveness as well.

Results of the Edinburgh European Council

The European Council meeting in Edinburgh (11 and 12 December 1992) provided the impetus for continued European integration within the Maastricht framework. The financial aspects covered were:

- the amount of own resources to allocate to the Community;
- the structure of budget financing;
- the development of expenditure in each main category.

It also set guidelines for:

- budgetary discipline;
- the Cohesion Fund to be established;
- borrowing/lending operations for structural measures;

³ Note that, for the ACP countries, development policy comes under the European Development Fund which is outside the general budget.

⁴ For a detailed description of the 1988 agreement see P. Zangl: The Interinstitutional Agreement in Budgetary Discipline and Improvement of the Budgetary Procedure, in: Common Market Law Review, Vol. 26 (1989), pp. 675-678.

the budgetary treatment of loan guarantees to non-member countries.

The Council (General Affairs) had previously adopted a common position on a new Interinstitutional Agreement at its meeting on 7 December 1992 .

Expressed as a percentage of GNP, the own resources ceilings for each year between now and 1999 are as follows:

1993	1994	1995	1996	1997	1998	1999
1.20	1.20	1.21	1.22	1.24	1.26	1.27

The corresponding ceiling on commitment appropriations is set at 1.335% of GNP in 1999.

The Protocol on Economic and Social Cohesion in the Maastricht Treaty invites the Member States to "take greater account of the contributive capacity of individual Member States in the system of own resources, and examine means of correcting, for the less prosperous Member States, regressive elements existing in the present own resources system".

In Edinburgh, the European Council agreed:

- to gradually reduce the VAT call-in rate from 1.4% to 1.0% between 1993 and 1999;
- with effect from 1995, to cap the VAT base of the four Cohesion Fund countries at 50% of their GNP and to phase

in the same measure for the other Member States between 1995 and 1999.

On the basis of the graduated application proposed, the Commission's objectives should be attained by 1999, when VAT should account for less than 35% and the GNP resource should be financing nearly half the budget.

The formula for correcting the United Kingdom's budget imbalance was retained.

In its conclusions, the European Council placed expenditure in the context of continued budgetary discipline. It pronounced in favour of a new budgetary discipline decision based on the experience acquired, the continued application of the cost-effectiveness principle, and the renewal of the Interinstitutional Agreement. The financial perspective adopted by the European Council in Edinburgh is given in Table 2.

This financial perspective complies with the requirement that the own resources ceiling remain at 1.20% of GNP until 1994 because of the slowdown in economic activity and the resulting constraints on government finances.

Comparison with Earlier Periods

Analysis of expenditure during the period covered by the financial framework established in Edinburgh, in comparison with the two previous periods (1984-1988 and

Table 2
Financial Perspective
Appropriations for commitments
(million ECU – 1992 prices¹)

	1993	1994	1995	1996	1997	1998	1999
1. Agricultural guideline	35 230	35 095	35 722	36 364	37 023	37 697	38 389
2. Structural actions	21 277	21 885	23 480	24 990	26 526	28 240	30 000
– Cohesion Fund	1 500	1 750	2 000	2 250	2 500	2 550	2 600
– Structural Funds and other operations	19 777	20 135	21 480	22 740	24 026	25 690	27 400
3. Internal policies	3 940	4 084	4 323	4 520	4 710	4 910	5 100
4. External action ²	3 950	4 000	4 280	4 560	4 830	5 180	5 600
5. Administrative expenditure	3 280	3 380	3 580	3 690	3 800	3 850	3 900
6. Reserves	1 500	1 500	1 100	1 100	1 100	1 100	1 100
– Monetary reserve	1 000	1 000	500	500	500	500	500
– External action							
= emergency aid	200	200	300	300	300	300	300
= loan guarantees	300	300	300	300	300	300	300
Total appropriations for commitments	69 177	69 944	72 485	75 224	77 989	80 977	84 089
Appropriations for payments required	65 908	67 036	69 150	71 290	74 491	77 249	80 114
Appropriations for payments (% GNP)	1.20	1.19	1.20	1.21	1.23	1.25	1.26
Margin for unforeseen expenditure (% GNP)		0.01	0.01	0.01	0.01	0.01	0.01
Own Resources Ceiling (% GNP)	1.20	1.20	1.21	1.22	1.24	1.26	1.27

¹ The inflation rate applicable for the budget is 4.3%. ² Total external expenditure 1993: 4 450; 1994: 4 500; 1995: 4 880; 1996: 5 160; 1997: 5 430; 1998: 5 780; 1999: 6 200.

1988-1992) reveals a steady decline in the rate of increase and gives evidence of the consistency in the priorities set.

Table 3 gives the figures for the 1984 budget and, for the other years, the ceilings in the financial perspective.

Comparing like with like, i.e. after removing the effect of the special measures for the UK in 1984, the increase in total commitment appropriations (in 1992 prices) over the three periods is:

1984-1988:	+ ECU 14 billion, an average annual growth rate of 7.6%
1988-1992:	+ ECU 12 billion, an average annual growth rate of 5%
1992-1999:	+ ECU 17 billion, an average annual growth rate of 3.3%.

It can be seen that the rate of growth of commitment appropriations over the three periods has declined steadily. No doubt this comes partially from the increased basis amount in each case, but it has also to be seen as a reliable indicator of improved budgetary discipline, especially in the field of agricultural expenditure.

Table 3
Development of Expenditure 1984-1999

(billion ECU – 1992 prices)

	1984	1988	1992	1999
EAGGF (Monetary reserve)	26.9	33.5 (1.0)	35 (1.0)	38.4 (0.5)
Structural	7.1	9.8	18.6	30
Internal	2.1 ^a	2.3	3.9	5.1
External (Reserves)	1.4	1.5	3.9	5.6 (0.6)
Administration	1.9 ^b	2.4 ^b	3.2 ^b	3.9
Total commitments	41 ^a	55	67	84
Total payments	39	53.5	64	80

^a The amounts of the special measures for the UK have been removed from the figures. ^b The cost of stock disposal measures and any refunds to Spain and Portugal are not taken into account in this amount, but in overall totals.

Table 4
**Share of Each Category in the Total of
Commitment Appropriations**
(in percent)

	1984	1988	1992	1999
EAGGF + monetary reserve	65.6	62.7	53.7	46.3
Structural	17.3	17.8	27.8	35.7
Internal	5.1	4.2	5.8	6.1
External (+ reserves)	3.4	2.7	5.8	6.6 (7.4)
Administration	4.6	4.4	4.8	4.6

However, these rates are still higher than the average annual GNP growth rates for each of these periods:

1984-1988:	+ 1.9% per year
1988-1992:	+ 2.4% per year
1992-1999:	+ 2.3% per year (estimated).

In 1992 prices, payment appropriations have accounted for an increasing proportion of GNP since 1984, although the rate of increase has been falling steadily:

1984:	0.85%
1988:	1.09%
1992:	1.18%
1999:	1.26%.

Compared to the growth rate of GNP, the Community budget had its strongest increase at the beginning of the eighties, when GNP growth was lower and before a systematic budget discipline was defined and decided by the European Council in Brussels in 1988.

Table 4 shows that:

□ the share of agricultural expenditure has begun to drop, even before the introduction of budgetary discipline and the decision on the agricultural guideline, after which it fell at a faster rate;

□ there has been a substantial increase in the proportion of the budget devoted to structural expenditure since 1988. This is chiefly a consequence of the political choices made in 1988 (doubling the allocation for the structural Funds between 1987 and 1993) and the creation of the Cohesion Fund by the Treaty on European Union.

These trends apart, there has been a steady increase in internal policy expenditure since 1988 as well as a significant rise in external expenditure.

Administrative expenditure by all the institutions as a proportion of total commitment appropriations has remained steady at below 5%.

Changes Affecting the Various Categories

The reduction in the margin for unforeseen expenditure to 0.01% means that the situation in which the new financial perspective has to operate is not only different but more constrictive than before and what will happen remains to be seen. Since then, expected economic growth slowed down further. Thus, for the time being this margin has virtually reduced to zero. That puts the financial decisions taken in Edinburgh in a different light to those taken in Brussels five years ago. Future developments will show whether it is possible or not to operate the Community budget correctly in such a narrow framework.

Category 1: The agricultural guideline is now to cover all CAP expenditure, i.e. including flanking measures. This means that, as was the case with the Commission's proposals, guideline coverage will be extended to:

- set-aside expenditure and income aids;
- expenditure under flanking measures (early retirement, environment, reforestation), including expenditure on related measures under Objective 5a of the structural Funds;
- expenditure under the Fisheries Guarantee Fund.

The Edinburgh conclusions are therefore consistent with the reformed CAP. However, the additional agri-monetary costs may eventually result in agricultural expenditure diverging from the guideline. Consequently, the operation of the monetary reserve will be extended to cover, if necessary, some of the agri-monetary costs over and above expenditure that is compatible with the guideline. As a last resort, additional funding outside the own resources ceiling may be needed.

Category 2: The allocations earmarked for Objective 1 of the structural Funds and for the Cohesion Fund are fairly

close to those proposed by the Commission. For the four Cohesion Fund Member States, this should permit a doubling of commitments under Objective 1 between 1992 and 1999. On the other hand, the growth in the allocations for the other objectives will be slower than before.

The exact distribution of these allocations and the annual increases will depend on the application of the basic regulations to be adopted for the structural Funds and the Cohesion Fund.

Category 3: The ceiling for internal policies is set to rise relatively slowly (+ 3.9% a year on average, or 31% over the seven-year period), for the following three types of expenditure:

- research,
- trans-European networks (TEN),
- other internal policies.

On research and its link with enhanced economic competitiveness, the European Council took the view that this was not to be seen as a priority in Community policy. In consequence, the amounts agreed in Edinburgh remain far below the ones proposed by the Commission,

Jill Rubery/Jill Earnshaw/Brendan Burchell

New Forms and Patterns of Employment: The Role of Self-Employment in Britain

This research constitutes the UK contribution to an international socio-legal research project entitled „New forms and conditions of employment: the development of the legal and regulatory framework for the labour market“.

The report explores the relationship between the growth of self-employment and the changing patterns of industrial and social organisation, legal regulation and state policy, and hence examines the conditions which could explain its growth. The report recognises that self-employment in fact spans a variety of forms of autonomous working, from independent entrepreneur to the most dependent forms of own account workers such as homeworkers, and therefore begins by assessing the extent to which the legal determination of employment status recognises such diversity and is able to accommodate it. After considering particular aspects of female self-employment, and questioning such notions as the existence of a natural tendency of ethnic groups to entrepreneurship, the report concludes by examining the relationship of self-employment to the growth of small firms and to government policy.

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obviously based on a different assessment of subsidiarity for this kind of policy. Beyond the implicit margin for increasing Research and TENs, the moderate increase in this category shall permit growing efforts in fields like the implementation of the internal market, education, vocational training and environment.

Category 4: The 42% increase for external action – nearly 60% if the reserves are included – should enable the Community to strengthen its presence in most of the geographical areas concerned. The pronounced tendency for expenditure for external policies to grow is linked to the measures in favour of Central and Eastern Europe as well as of CIS. At the same time, the correct budgetary treatment of the guarantee risk involved in borrowing/lending operations outside the Community and the ability to rapidly mobilize an emergency aid reserve should make it that much easier for the Community to meet its various commitments.

Category 5: Expenditure on pensions aside, the increase in the administrative resources available to the institutions may not exceed 1.8% per year on average over the period. Moreover, the non-pension expenditure ceiling will remain unchanged between 1997 and 1999.

Assuming a similar administrative expenditure pattern for all the institutions, the Commission's total annual allocations should increase by ECU 250 million between 1992 and 1999. This will do no more than keep staff numbers, buildings and other administrative costs more or less at their current levels.

Implementing the Decisions

Legislation will have to be enacted to give effect to the conclusions of the Edinburgh European Council. The main instruments are as follows:

- An updated budgetary discipline decision dealing primarily with discipline on agricultural spending. The updating will have to ensure the continuation of the existing arrangements with appropriate improvements based on experience gained so far. Detailed provisions will also be included for the revised operation of the monetary reserve, the mechanisms governing the reserves for emergency aid and loan guarantees and the application of the guarantee given by the Edinburgh European Council to cover agri-monetary expenditure resulting from realignments which could not be covered within the financial perspective.
- A regulation on the Guarantee Fund to cover the risks involved with loans outside the Community.
- A new own resources decision setting the new ceilings

on own resources and the arrangements for financing the Community budget.

As these instruments are the translation into legal terms of the pledges made in Edinburgh, ways should be found of adopting all of them before the end of 1994. The own resources decision will also need to be ratified by the Member States.

But finalizing these instruments will not be enough to give practical effect to the conclusions of the Edinburgh European Council: Parliament, the Council and the Commission will have to conclude a new Interinstitutional Agreement which, as in 1988, will determine how these conclusions are to be applied in budgetary terms. There are, unfortunately, a number of obstacles blocking this Agreement, and it is by no means certain that they can be cleared away quickly. The benefits, however, are manifold:

- financial security for the Community;
- budgetary peace, which is a *sine qua non* for a positive image of the Community and for the cost-effective utilization of the appropriations entered in the budget in compliance with the principle of annuality;
- joint decision by the three institutions on the allocation of Community resources between the main groups of policies.

The main difficulty derives from the fact that if the payment appropriations are to be kept below the own resources ceiling – held at 1.20% of GNP for 1994 – the figures agreed at Edinburgh give a margin for increasing non-compulsory expenditure which is less than Parliament would enjoy under Article 203(9) of the Treaty. Although the Edinburgh figures for the remainder of the period are far higher than what would result from application of Article 203(9) year by year, Parliament is not at all keen to accept this. Other factors of uncertainty are the planned enlargement of the Community, the particularly uncertain economic outlook, the election of a new Parliament in 1994 and the installation of a new Commission in 1995. These affect not only the figures but also the institutional aspects of Community integration.

The outcome of the European Council in Edinburgh allowed Parliament to decide the 1993 Budget in due time a few days later, giving the Community another year of budgetary peace to address its more fundamental problems. The coming months will show whether the Community is going to be faced with a fresh series of annual budget clashes and all the attendant dangers, or whether all parties will be convinced of the benefits the Community and its institutions will derive from an Interinstitutional Agreement, even at the cost of some concessions and voluntary restraint.