

TRENDS IN THE INTERGOVERNMENTAL FISCAL RELATIONS IN THE EUROPEAN UNION

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Abstract: *The study aims to present the different interpretations of the fiscal federalism and its connection with the regional policy of the EU – a field which has unfortunately remained relatively neglected in the legal literature so far. Within the framework of fiscal federalism we are doing research on the concerning disposal of the Treaty of Lisbon, the main recent preparatory acts and other documents. With the knowledge of the theory of fiscal federalism we could create a special systematic, coherent scheme to analyze the regional policy of the European Union.*

Key words: *Fiscal federalism, intergovernmental fiscal relations, regional policy, financial framework, Treaty of Lisbon, territorial cohesion, Territorial Agenda, Green Paper of the Commission, progress reports on economic and social cohesion*

The intergovernmental relations and multi-level governance are a popular topic both in the European and Hungarian researches, mainly in the political and economic studies. One of the special parts of this field is the system of intergovernmental fiscal relations (or fiscal federalism) – a field which has unfortunately remained relatively neglected in Hungarian legal literature so far. In a nutshell, the theory of fiscal federalism focuses primarily on *the various functions of state finances* (like allocation, redistribution and stabilization), *the roles and governmental levels* on which these functions can be accomplished the most effectively, and finally, *the fiscal resources and tools* necessary to successful achievement.¹

In *the early stage of the researches concerning the fiscal federalism* focused only on the federal systems and claimed that the distribution and stabilization branches of public fiscal department must perform their functions primarily at the central-government level. In contrast, in the allocation branch local government as well as the central government, has important responsibilities in the provision of needed public goods and services.²

One of the recent tendencies of fiscal federalism is fiscal decentralisation, examining the system of financial relations between the various governmental levels in the framework of the European Union – extending thus the scope of research from intergovernmental fiscal relations of federal states to the *various financial decentralisation processes and instruments (e.g. taxes, aids, dues) of the member states*.³ This aspect of fiscal federalism has already been discussed in numerous dissertations related to the *topical research of international organisations*.⁴ With the acceptance of the European Charter of Local Self-Government, the Council of Europe committed itself to the research of financing the modernization of exercising public services. In Strasbourg, under the guidance of the European Committee on Local and Regional Democracy of the Council

¹ The connection literature for example: Musgrave, R. A.–Musgrave, P.B. (1973). *Public Finance in Theory and Practice*. New York: McGraw-Hill. Oates, W. (1972) *Fiscal federalism*. New York: Harcourt Brace Jovanich. Oates, W. (1991) *Studies in Fiscal Federalism*. Aldershot, Hants, England; Brookfield, Vt., USA: E. Elgar.

² Oates, W. (1968) *The Theory of Public Finance in a Federal System*. Canadian Journal of Economic (February 1968), p. 54.

³ The connection literature for example: Bosch, N–Durán, J.M. (2008) *Fiscal Federalism and Political Decentralization*. Cheltenham, UK; Northampton, MA, USA: E. Elgar. Fossati, A.–Panella, G. (1999) *Fiscal Federalism in the European Union*. London: Routledge. Rattso, J. (ed.) (1998) *Fiscal federalism and state-local finance: the Scandinavian perspective*. Cheltenham, UK; Northampton, MA, USA: E. Elgar.

⁴ The connection literature for example Bosch, N–Durán, J.M. (2008) *Fiscal Federalism and Political Decentralization*. Cheltenham, UK; Northampton, MA, USA: E. Elgar. Fossati, A.–Panella, G. (1999) *Fiscal Federalism in the European Union*. London: Routledge. Rattso, J. (ed.) (1998) *Fiscal federalism and state-local finance: the Scandinavian perspective*. Cheltenham, UK; Northampton, MA, USA: E. Elgar.

of Europe, the dedicated Committee of Experts on Governance and Resources deal with, among others, issues related to and challenges resulting from the modernization of financing local governments.⁵ Besides, in 2003 the OECD established a network of professionals dealing with the operation of fiscal relations across governmental levels. Further the European Union (experts from the EU member states) treats the issue of financing local authorities and local fiscal autonomy within the framework of the Paris seminar held in December 2008.

The *most recent studies of fiscal federalism* (a topic I am also preoccupied with currently) inspect the realization of intergovernmental fiscal relations in the framework of the European economic field. In other words, this approach is engaged in finding out how the new, special governmental level of the European Union affects the traditional level of member states, which functions of public sector can be ensured by the EU and what consequences does this new level carries in itself.⁶ These researches emphasise the importance of the monetary and regional policy of the Union. In my opinion the functions of public finance are realised in a characteristic way in view of the EU and the member states. The provision of allocation function (take into consideration the most important and traditional governmental expenditures as public health, education and social system, which fall within the competence of the member states) is not typically performed in the level of the EU. Nevertheless the redistribution branch is provided by the support policy of the EU, preliminary by the regional policy.⁷ The stabilization function is – although in a limited way – rather guaranteed by the monetary policy of the EU instead the fiscal policy of it. According to the Treaty of Lisbon Article 3.b the limits of Union competences are governed by the principle of conferral. Under the principle of conferral, the Union shall act only within the limits of the competences conferred upon it by the member states in the Treaties. The use of competences is governed by the principles of subsidiary and proportionality. Hereby we can claim that, although the role and the competence of the European Union is expanding, but because of the limitation of competences and the dependant on the authorization given by the member states, it results a *special, inverse federation system*.

It is to be noted that we should make *differences between the intergovernmental and intergovernmental relations* in the EU and its member states. If we approach the EU as a traditional international organisation, the Union has only limited and external effect on the different governmental levels of member states. In this case we have to use the intergovernmental phrasing. But if we accept the recognition as the EU is a supranational organisation – a special but still not entirely developed community – we should deal with the intergovernmental term (as I did). In the aim of avoidance the misunderstanding, I assign the same semantic content to these two terms in this study.

Hereinafter we deal with the fiscal tendencies according to the European regional policy, which accomplishes most of all the distribution branch.

In the European Union the regional policy is changing, at least a new financial framework is passed. It was so at the latter budget, at the time of acceptance the 2007-2013 financial framework.⁸ But more questions have arisen: Are these changes significant? Are there any underlying essence? What kind of problems exists in the recent system? What can be expected in 2007-2014?

The Treaty of Lisbon, among others, modified the rules of the budget (art. 270/a, 272.) and dispose about the territorial cohesion (art. 2. point 3.). It is one of the aims of the EU. The territorial cohesion is increasingly important within the union. In Leipzig, 2007 on the 24-25th of May, the

⁵ Csupa, M.-Vigvari A. (2009) *International experience concerning the development of local finance*. In: Public Finance Quarterly, 2009/2-3. number p. 466.

⁶ See Vaneecloo, C.–Badriotti, A.–Fornassini, M. (2006) *Fiscal Federalism in the European Union and Its Countries*. Brussels, P.I. E. Peter Lang. Baimbridge, M.–Whyman, P. (2004) *Fiscal Federalism and European Economic Integration*. London: Routledge.

⁷ In my opinion the agricultural policy – through the increasing part of the rural development – has some redistributive attribute, too.

⁸ Further details in Csűrös, G. (2007) *The changing subvention policy in the aspect of the 2007-2013 budget, and the effect of changes on the financing of local government*. In: Horváth, M. T. (ed.) *Views and appearances. Decentralization in the aspect of financing*. Budapest: KSzK. 2007. pp. 101-144.

Territorial Agenda was passed by the ministries of the territorial development, and they asked the European Commission to prepare the Green Paper on Territorial Cohesion.

In October 2008, the European Commission adopted a Green Paper on “Territorial Cohesion”⁹ launching a broad public debate on territorial cohesion and its policy implications. The Commission was pleased to receive 391 responses¹⁰. The Green Paper and the connecting opinions are important, because they focus the dilemmas of the regional policy.

The first general conclusion which can be drawn from the discussion is the recognition by stakeholders of the important role cohesion policy plays in the construction of the European Union and the support for continuation of that policy. *Any attempt to re-nationalise the policy is almost unanimously rejected.*¹¹

All contributions agree that the main objective of cohesion policy is the reduction of economic and social disparities between the levels of development of European regions. Lagging regions must thus remain the focus of the policy. Yet, a majority of contributions – along with the European Parliament – argues that the policy should cover the whole territory of the EU,¹² to say the territorial cohesion policy should support the developed regions too. The emphasize of this is not gratuitous. The financial priorities of the EU were questioned by the changes of the heads of the 2007-2013 financial framework. The agricultural expenditure (371 344 million euro /pro 7 years) was the first title, but from 2007 it has become the second head. The “winner” was the structural policy (308 139 million euro /pro 7 years). So we could see, that not the structural policy takes it all! The first title, the sustainable development contains another, new head: the support of the competitiveness (74 098 /pro seven years). The connection and a more unified handle of these two policies is also supported by the forth progress report on economic and social cohesion.¹³ This aim could have two kinds of meaning. Firstly if the resources of the regional policy expand, it could strengthen the redistribution function among the EU and the member states. But the expenditures subsidize the competitiveness have an opposite effect, it can reduce the redistribution character.

A significant majority of stakeholders (concerning the Green Paper of the Commission) calls for further *clarification in the allocation of responsibilities between the different institutional levels* (Commission, Member State, regions and other players). Many stakeholders, particularly at the regional and local level, would appreciate further *decentralisation of responsibilities*.¹⁴

The majority of contributions underline the importance of *coordinating* national and regional strategies, regulations and funding.¹⁵ This opinion concerns coordination between cohesion policy, other Community policies, and national policies.

And what kind of financing suggestions have arisen?

Another important matter frequently mentioned concerns the coordination among the European Regional Development Fund, the European Social Fund and the Cohesion Fund. Besides the principle of the “one fund one program” – adopted from 2007 – make the accomplishment of the regional policy more difficult. Therefore some contributions call for the integration of the three fund into *a single fund* for the sake of a more coherent strategic development.

A number of contributions insist on further exploring the use of means of *financing other than grants* such as *bank loans, micro-credits, risk capital instruments or public-private partnership instruments*.

The problem is that the traditional public authorities dealing with the allocation of regional subsidies are neither concerned nor competent to authorize and decide upon repayable assistances. However the EU supports the use of these indirect financial assets, the legislation, decision making organ and the applicant prefer to avoid them. It would worth to take into consideration the German

⁹ COM(2008) 616 final

¹⁰ http://ec.europa.eu/regional_policy/consultation/terco/consultation_en.htm

¹¹ COM(2008) 371 final p. 4.

¹² COM(2008) 371 final p. 4.

¹³ COM(2006) 281 final

¹⁴ COM(2008) 371 final p. 7.

¹⁵ COM(2009) 295 final p. 13.

example. The Bank für Wiederaufbau is an institution under state control the state, but operating as a profit-orientated, financial business unit.

And actually, the opinions seem to be divided regarding the *opportunity to use cohesion policy as an instrument to react immediately to asymmetric shocks* or important crises triggered by processes of restructuring: while some advocate more flexibility, others point out that cohesion policy is first and foremost a structural policy characterised by strategic planning with a medium and long-term perspective.

In the Opinion of the European Economic and Social Committee (EESC) on the Green Paper the *(re)establishment of Community initiative programmes* was emphasized.¹⁶

The subsidiarity and the proportionality are fundamental principal in the Union, and fiscal data covering recent decades for a large number of countries indicate a growth on the budgets of decentralized levels of government relative to that of the national authority.¹⁷ But in the same time the European Community brings the centralization of a number of economic functions (agriculture, rural development, regional policy, customs policy etc.). New levels of government and new forms of public agencies are coming into being in a process of fiscal evolution and the actions of various levels of government interacting with one another.¹⁸ These changes give reason to research the intergovernmental fiscal relations in the European Union.

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12. <http://eur-lex.europa.eu>

¹⁶ 2009/C 228/24 point 3.9.1

¹⁷ Oates, W. (1977) *An Economist's perspective on Fiscal Federalism*. In: Oates, W. (ed.) The Political Economy of Fiscal Federalism. p. 3.

¹⁸ Oates, W. (1991) *Studies in Fiscal Federalism*. Aldershot, Hants, England; Brookfield, Vt., USA: E. Elgar.

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