

## Fiscal Consolidation Processes In The European Union\*

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**ABSTRACT.** The essence, the stages of formation and development of the budget system of the European Union (EU) are revealed herein, as well as the main directions and mechanisms of consolidation of the national budget of Member States. The role and place of the EU budget in the system of economic relations of integration association, sources of formation and targeted uses of the common budget. On the basis of the EU legal acts and research of Ukrainian and foreign scholars the principles and general rules were analyzed which govern the budget process, the essence and main reasons of inconsistency of interbudget relations in the EU. The organization and the problems of institutional cooperation in the budgetary system of the EU are studied as well as their impact on the budget policies of the EU and the Member States. Revenues and expenditures of the EU budget, their dynamics, structure, efficiency and role of regional development in the Community were analyzed as well. A mathematical calculation of projected trends of interbudget relations was made, and the author's vision of application of specific mechanisms and instruments in the EU budget process was motivated herein.

**KEYWORDS.** European Union, national budget, budget system, fiscal consolidation, financial and budgetary policy, budgeting process, inter-budget relations, in-come, expenditures, member states.

### Introduction

Creation of own budget within the system of interstate integration associations of the EU was the beginning of a full-fledged supranational financial system which requires a change in approaches to scientific-methodological motivation and practical application of new models of institutional interaction with the EU. The slowdown of economic growth in many countries that occurred in the early twenty-first century was no signal either for the EU or for other leading countries of the world economy, for the immediate counteraction to development of crisis in the

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global financial system.

At the same time, constantly growing imbalance of financial market made it impossible to apply effective regulators of commodity market and monetary policies of the EU because of the lack of their proper interaction with fiscal consolidation measures at national, regional and global levels. The process of fiscal consolidation of integration association is the new phenomenon in the system of interbudget relations of supranational financial system, which has no sufficient scientific-theoretical justification for the integrity of institutional financial environment, the budgeting process, and convergence of areas of integration financial policy. Under these conditions the common EU budget can only be used as a source of financing common commodity market and alignment of the socio-economic situation of member countries, but in conjunction with monetary mechanisms the budget has the role of the main regulator of balance of macroeconomic policy and supranational financial system of the EU as a whole.

Processes of fiscal consolidation in the European Union have been studied in works of such Ukrainian and foreign scholars, as Andriushchenko V.<sup>2</sup>, Barrios S.<sup>3</sup>, Blinder A.<sup>4</sup>, Giavazzi F.<sup>5</sup>, Domenech R.<sup>6</sup>, Ehlers G.<sup>7</sup>, Zuiev V.<sup>8</sup>, Kudriashov V.<sup>9</sup>, Leen A.<sup>10</sup>, Lukianenko D., Poruchnyk A., Stoliarchuk Ya.<sup>11</sup>, Liutyi I.<sup>12</sup>,

<sup>2</sup> *Andriushchenko V.L., Danilov O.D.* Tax systems of foreign countries. Study guide / V.L. Andriushchenko, O.D. Danilov // K.: Computer press, 2004. – P. 300. [In Ukrainian].

<sup>3</sup> *Barrios S., Langedijk S., Lucio Pench L.* EU fiscal consolidation after the financial crisis Lessons from past experiences / S. Barrios, S. Langedijk., L. Pench. – European Commission Directorate General for Economic and Financial Affairs. - Economic Papers 418 1 July 2010. – [Electronic resource]. Access mode: [http://ec.europa.eu/economy\\_finance/publications/.../pdf/ecp418](http://ec.europa.eu/economy_finance/publications/.../pdf/ecp418)

<sup>4</sup> *Blinder Alan C., Solow Robert M.* Does fiscal policy matter? / Econometric Research Program Research Memorandum No. 144 August 1972. [Electronic resource]. Access mode: <http://www.princeton.edu/~erp/ERParchives/archivepdfs/M144>

<sup>5</sup> *Alesina A., Giavazzi F.* The Future of Europe: Reform or Decline [Electronic resource]. Access mode: [http://books.google.com/books/about/The\\_Future\\_of\\_Europe.html?id...](http://books.google.com/books/about/The_Future_of_Europe.html?id...)

<sup>6</sup> *Domenech Rafael, Maudes Antonio and Varela Juan.* Fiscal Flows in Europe: the Redistributive Effects of the EU Budget, *Weltwirtschaftliches Archive*, 136(4), 2000. – [Electronic resource]. Access mode: <http://www.uib.cat/depart/deaweb/personal/profesores/personalpages/joanrossello/Docencia/Aplicada/domenech>.

<sup>7</sup> *Gerd Ehlers.* State debt management: tasks, objectives, participants / Finance of Ukraine. – 2014. – No. 1. – P. 7 – 21. [In Ukrainian].

<sup>8</sup> *Zuiev V.* EU: supranational mechanism – main tool of European integration? / *Modern Europe*. 2011. No. 2. P. 94-108. – [Electronic resource]. Access mode: [http://91.190.232.206:8080/period11/SovrEvropa/SovrEvropa\\_11\\_02.doc](http://91.190.232.206:8080/period11/SovrEvropa/SovrEvropa_11_02.doc). [In Russian].

<sup>9</sup> *Kudriashov V.P.* Fiscal consolidation and its effects // *Economics of Ukraine*. – 2011. – No. 9 (622). – P. 31 – 46. – [Electronic resource]. – Access mode: <http://www.un.org/en/development/desa/policy/wesp/index.shtml>. [In Ukrainian].

<sup>10</sup> *Leen A.R.* 'The Revenues of the European Union: Past, Present, and Future', in: *International Relations, Culture and Global Finance*, D. Kalaitzidis (ed.), ATINER, 2011. – [Electronic resource]. Access mode: <http://media.leidenuniv.nl/legacy/al-2011-05>.

<sup>11</sup> *Lukianenko D.H., Poruchnyk A.M., Stoliarchuk Ya.M.* International economics: manual / D.H. Lukianenko, A.M. Poruchnyk, Ya.M. Stoliarchuk // K.: KNEU, 2014. – P. 762. [In Ukrainian].

<sup>12</sup> *Liutyi I.O., Demydenko L.M., Romaniuk M.V. et al.* Tax system: Study guide for students of higher educational establishments. Study guide for students of higher educational establishments. Edited by Liutyi I.O. / I.O. Liutyi, L.M. Demydenko, M.V. Romaniuk, et al // K.: Centre of Educational Literature, 2009. – P. 456. [In Ukrainian].

Oates W.<sup>13</sup>, Pisani-Ferry J.<sup>14</sup>, Renwick R.<sup>15</sup>, Sydorova O.<sup>16</sup>, Sokolovska A.<sup>17</sup>, Toloknova T.<sup>18</sup>, Tuhan-Baramovskyi M.<sup>19</sup>, Tilai C.<sup>20</sup>, Hix S.<sup>21</sup>, Chuzhykov V.<sup>22</sup>, and many others.

Subject to the above, the purpose of our study is the theoretical motivation of the institutional environment of the EU fiscal consolidation under conditions of supranational financial system formation, the degree of convergence of budgeting process and its interaction with other parts of the system and the effectiveness of practical application of the Maastricht criteria.

### Main Part

The financial policy of the European Union (EU), as opposed to national financial policies of its members at the international level defines a set of objectives and system of measures of governing institutions of the bloc in financial sector to ensure financial stability based on the following key principles: stable prices, sound public finances and monetary conditions provided a stable

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<sup>13</sup> Oates W. E. Fiscal federalism and European union: some reflection / IL Futuro Dei Sistemi DI Welfare Nazionali Tra Itegrazione Europea E Decentramento Regionale coordinamento, competizione, mobilità Pavia, Università, 4 – 5 ottobre 2002/ [Electronic resource]. Access mode: <http://www.siepweb.it/siep/images/joomd/1398076615132>.

<sup>14</sup> Pierre Jacquet and Jean Pisani-Ferry Economic policy co-ordination in the Eurozone: what has been achieved? What should be done? /Sussex European Institute University of Sussex. – SEI Working Paper No. 40. – [Electronic resource]. Access mode:<http://www.sussex.ac.uk/sei/documents/sei-working-paper-no-40>

<sup>15</sup> Renwick Robin, The Lord Renwick of Clifton. "What Margaret Thatcher would be doing about Europe". New Direction - The Foundation for European Reform. December 2013, - Brussels, Belgium. – [Electronic resource]. Access mode: <http://newdirectionfoundation.org/content/what-would-margaret-thatcher-be-doing-about-europe>

<sup>16</sup> Sydorova E.A. Peculiarities of budgeting policy in the European Union: Article thesis / E.A. Sydorova. – M.: IMEO RAN, 2012. – P. 129. – [Electronic resource]. Access mode: <http://www.imemo.ru/files/File/ru/publ/2012/12030>. [In Russian].

<sup>17</sup> Sokolovska A.M., Rainova L.B. Tools for fiscal consolidation policy and their impact on macro-economic processes / A.M. Sokolovska, L.B. Rainova // Finance of Ukraine. – 2014. - No. 4. – P. 64 – 82. [In Ukrainian].

<sup>18</sup> Toloknova T.B. Financial control of budget of Europe / T.B. Toloknova // SPO. – 2006. – No. 12. – P. 55 - 56. [In Russian].

<sup>19</sup> Tuhan-Varanovskyi M.I. Political economy. Popular course / M.I. Tuhan-Baranovskyi // K.: Scientific opinion, 1994. P. 262. [In Ukrainian].

<sup>20</sup> Tulai Constantin, Sabău-Popa Claudia Diana, (2009) Budgetary Consolidations in EU-12. The annals of the University of Oradea, Economic Sciences, Volumul III – Sectiunea: Finante, Banci si Contabilitate, Tom XVIII 2009 – Volumul III – Sectiunea: Finante, Banci si Contabilitate, p. 415-421. – [Electronic resource]. Access mode: <http://steconomice.uroadea.ro/anale/volume/2009/v3-finances-banks-and-accountancy/69>.

<sup>21</sup> Hix S. The Political System of the European Union / S. Hix // The European Series. – Palgrave Macmillan. – 1999. – [Electronic resource]. Access mode: <http://www.lse.ac.uk/researchandexpertise/experts/profile.aspx?...s.hix%40lse>.

<sup>22</sup> Chuzhykov V.I. Global regional studies: History and Modern Methodology: Article thesis / V.I. Chuzhykov // K.: KNEU, 2008. – P. 272. [In Ukrainian].

balance of payments (Articles 119, 120)<sup>23</sup>. An important component of this policy is its budget component.

Unlike national budgetary policies aimed at the redistribution of countries' GNP for funding primarily social sphere, defense of the state, and implementation of priority economic programs, budget policy of integration grouping is aimed at accumulation of portion of national budgets funds and other financial resources for financial support for the implementation of the regional policies common for all the all member countries of the bloc. Now, subject to the Lisbon Treaty (2009), the powers of governments and institutions of the EU are divided into exclusive, shared and supporting competences. Exclusive competence, for the fulfillment of which the EU institutions are responsible, includes implementation of monetary policy, customs union, competition policy, and so on. The joint competence includes areas that are simultaneously regulated by both EU institutions and member governments, they are: social, transport, agricultural, environmental, and other policies. Exercise of powers within supporting competencies that is implemented by means of consultation, coordination, and financing mechanisms contributes to the development of education, culture, industry, tourism, etc<sup>24</sup>.

The budget component of the EU economic policy, unlike monetary policy, is mainly attributed to the powers of Member States, and therefore in the current founding treaties it has no legislative provisions, but is merely indicated as "financial regulations" governing the budgetary relations of Members States with respect to the common EU budget. Meanwhile, the issue of prioritization of budgetary control tools was repeatedly raised ever since the proposals of the "Werner Plan" (1971), which was supposed to introduce unified budget system of the Union. Within the scientific approach European integration system is identified as federalism, and therefore the principle of fiscal federalism is considered a basic principle of the EU budget system. In this context, the results of research conducted by scientists from the US and European countries help conclude that the low efficiency of influence of public finance instruments on the condition of the common market of the Union is the result of a fairly low supranational budget component of the EU financial system, which is 0.7% of combined budgets of member

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<sup>23</sup> Consolidated versions of the European Union Treaty and the Treaty on the Functioning of the European Union (2010/C 83/01)/30.3.2010 UA Official Journal of the European Union – [Electronic resource]. Access mode: <http://www.minjust.gov.ua/file/23491>. (date of addressing: 04.10.2014). [In Ukrainian].

<sup>24</sup> *Lukianenko D.H., Poruchnyk A.M., Stoliarchuk Ya.M.* International economy: Manual /D.H. Lukianenko, A.M. Poruchnyk, Ya.M. Stoliarchuk. – K.: KNEU, 2014. – P. 582. [In Ukrainian].

states. The EU budget system requires application of harmonized and mandatory rules of budgetary control over national budgetary policies which were first proposed in the Delors Package-1 (1986)<sup>25</sup> and found its continuation in the Stability and Growth Pact of 1997<sup>26</sup>.

The EU budget, the main institute of budgetary policy of the Union, as an economic category is a plan of formation and utilization of centralized fund of financial resources, and as a social category – a set of economic relations between the EU and its member states to ensure the tasks and functions of supranational institutions of the EU. The combination of the EU budget and national budgets of member states forms the budgetary system of the bloc. It has a three-component organizational structure: the EU budget, national budgets, and regulatory institutions. According to Roman agreements of 1957 and taking into account the changes introduced by the Lisbon Treaty (2009), functioning of the EU budget system is based on the following fundamental principles:

1) unity and budget accuracy means that all income and expenses related to implementation of the EU Treaty are included into the EU budget when there are no extra-budgetary funds;

2) annularity – budget period is defined from January 01 to December 31 of the calendar year. Additional periods can be set in individual cases where they are needed only under the terms defined by the relevant Regulation (on the Financial Regulation applicable to the general budget of the European Communities);

3) universality means that all costs (income), coming to the EU budget are credited into the single budget fund of the EU;

4) specification provides for flexibility in management of relevant institutions (budget holders) on transfer of budgetary appropriations for classification the same for all;

5) equilibrium provides for matching revenues and expenditures of the budget and inadmissibility for the EU budget to cover its deficit by borrowings;

6) unit of account which provides for a single billing currency for the EU budget – the Euro;

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<sup>25</sup> Report on Economics and Monetary Union in the European Community / Committee for the study of Economic and Monetary Union. Jaguars Delors Chairman. 1989. P. 16. – [Electronic resource]. Access mode: [http://aei.pitt.edu/1007/1/monetary\\_delors](http://aei.pitt.edu/1007/1/monetary_delors). (date of addressing: 05.10.2014).

<sup>26</sup> Stability and Growth Pact / European Commission. – [Electronic resource]. Access mode: [http://ec.europa.eu/economy\\_finance/economic.../sgp/index\\_en](http://ec.europa.eu/economy_finance/economic.../sgp/index_en). (date of addressing: 06.10.2014). [In Ukrainian].

Stability and Growth Pact offered at the meeting in Dublin (Ireland) in 1996 and approved by the EU Council in 1997, giving reasons for problems of regulation of budget deficit, government debt, and other “convergence criteria” and setting relevant restrictions.

7) sound financial management sets that the budget is implemented based on principles of efficiency, economy, and effectiveness, calculated subject to indicators that enable real assessment of results;

8) transparency determines that the budget and any changes to it, as well as information on the budget implementation to be published in official publications of the EU<sup>27</sup>.

Principles of formation of the EU budget system, as compared with the principles of national budget systems, confirm a desire to preserve fiscal autonomy of Member States to the fullest extent possible, the basis of which is intrastate fiscal decentralization. However, the use of supranational mechanisms contributes to abrasion of boundaries, blur of fundamentals of the classic sovereignty. Subject to figurative definition of V. Zuiev, budgetary system of the EU could be described as "pre-federal structure."<sup>28</sup>

In terms of a common market and a highly centralized monetary and currency system of the EU effectiveness of budget leverages of impact on economies of member states remains inefficient and requires substantial improvement on modernization of basis of the budget system and institutional mechanisms of influence of the supranational budget regulation of national budgetary systems where central place belongs to the fiscal consolidation process. In our view, internationally the fiscal consolidation is a set of measures of common budgetary policy to "support of reliable and balanced growth, creation of effective jobs, and maintenance of economic and financial stability in the long run."<sup>29</sup> Fiscal consolidation is ensured by institutional and regulatory activities of the Union through harmonization, convergence and unification of the budget process, aimed at achieving the goal of financial policy of the EU (Fig. 1).

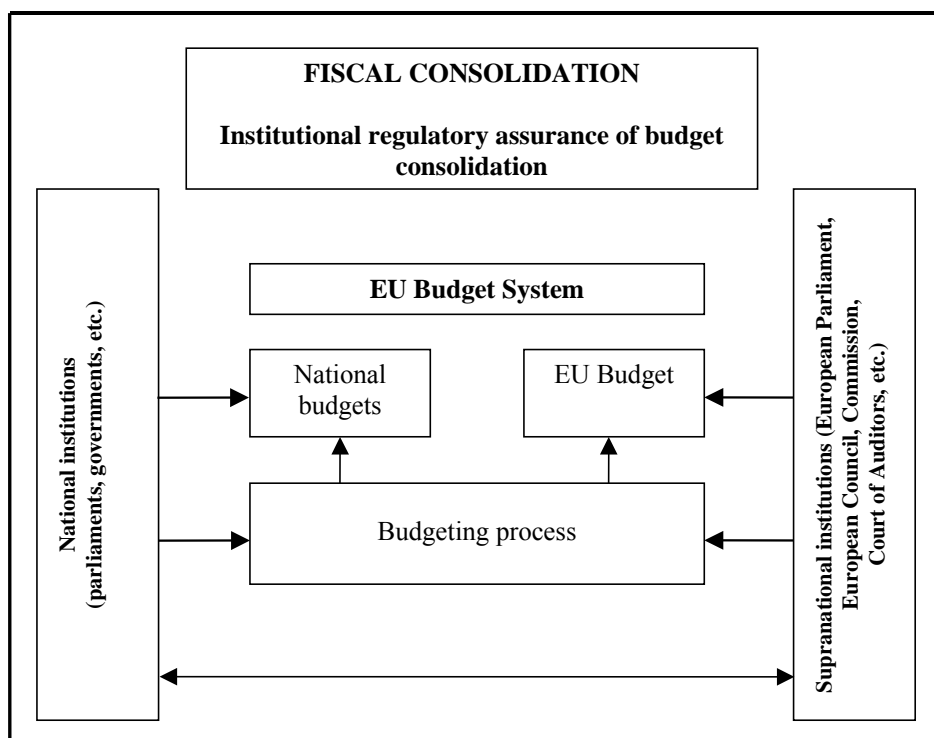
Given the fact that the budget process at the supranational level in the EU is the phenomenon that is unparalleled in history, and is radically different from the budget systems of national budget procedures, the need to strengthen its institutionalization arose. In this context, in the early 2000s the Sussex

<sup>27</sup> Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities / Official Journal of the European Communities (OJEC). 16.09.2002, n° L 248. [s.l.]. – [Electronic resource]. Access mode: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=2002R1605:20071227...> (date of addressing: 06.10.2014).

<sup>28</sup> Zuiev V. EU: supranational mechanism – main tool of European integration? / Modern Europe. 2011. No. 2. P. 94-108. – [Electronic resource]. – (date of access: 07.10.2014). – Access mode: [http://91.190.232.206:8080/period11/SovrEvropa/SovrEvropa\\_11\\_02.doc](http://91.190.232.206:8080/period11/SovrEvropa/SovrEvropa_11_02.doc) [In Russian].

<sup>29</sup> World Economic Situation and Prospects 2015 // United Nations publication Sales No. E.15.II.C.2. – New York, 2015. – [Electronic resource]. Access mode: <http://www.un.org/en/development/desa/policy/wesp/> (date of access: 02.02.2015)

European Institute, University of Sussex (Brighton, UK) as commissioned by the EU within the project Challenges for EU External Economic Policy in the Next Decade developed recommendations for strengthening economic policy coordination in the euro-zone, including institutional and procedural changes in the EU budgetary process. Proposals for the establishment of the Economic Policy Council among finance ministers of the euro-zone countries were formulated in order to develop recommendations on fiscal policies for member states (Von Hagen (1999) to provide the Euro Council, as the executive body, with the legislative functions (Dominique Strauss-Kahn (2000), and other structural changes.



**Fig. 1.** Structural logical framework of fiscal consolidation in the EU

Equally important were the proposals for the budget procedure in part of adopting structural changes in the fiscal and tax implications in the second half of the calendar year for the creation of conditions for their consideration when forming respective budgets to achieve full cooperation of EU procedures with national

decisions, establishment of effective monitoring and continuous updating of information throughout the year with respect to implementation of EU budgets. Considerable attention was paid to the introduction of new, more sophisticated convergence criteria as those that were used in 1997, known as the Maastricht criteria of economic convergence. They were introduced to assess the stability of participation in the economic and monetary union, but not for complications of membership terms for the countries of Central and Eastern Europe, and as recognition of challenges of "real convergence" that can be more severe for countries with very different initial conditions than for countries with the same level of development and with a long history of economic integration with the EU. Six institutional principles were offered which will enable coordination of economic policies of the EU and member states:

- 1) implementation of the economic policy charter;
- 2) greater transparency and predictability in economic policy;
- 3) conversion of the Euro-Group in a collegial executive body;
- 4) close cooperation between EU procedures and national decisions;
- 5) more efficient exchange rate policy;
- 6) monetary expansion strategy<sup>30</sup>.

Part of the proposed structural and procedural changes in the EU budgetary process was reflected only 7 years after in the Lisbon Treaty (2007), which provided for basic provisions of enhanced cooperation between the EU and its member states (Art. 20 of the consolidated version of the Treaty), the criteria for legislative approximation, economic policies coordination and rules of the budgeting process in terms of the EU budget. This was another step towards fiscal consolidation.

The budgeting process in the EU in terms of its complete procedure now includes legal regulation of preparation, consideration, acceptance (approval), implementation, reporting on budget execution and budget control. Preparation, consideration, and approval of the EU budget is carried out according to procedures established by the Treaty on the Functioning of the EU (TFEU Art. 313 – 314), Financial Regulations, rules of the Financial Regulation, orders of the Commission with respect to issues of

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<sup>30</sup> *Pierre Jacquet and Jean Pisani-Ferry* Economic policy co-ordination in the Eurozone: what has been achieved? What should be done? /Sussex European Institute University of Sussex. – SEI Working Paper No. 40. – [Electronic resource]. Access mode: <http://www.sussex.ac.uk/sei/documents/sei-working-paper-no-40>. (date of addressing: 09.10.2014).



the budget process<sup>31</sup>. If the budget is not adopted prior to the new fiscal year, current practice of monthly financing costs in the amount of no more than 1/12 of budget appropriations of the previous financial year applies provided that payments are provided for in the draft budget of the planning year (Art. 315 of the TFEU).

The mechanism of prospective financial forecasting introduced by the proposals set out in Delors Package-1, the Lisbon Treaty – Multiannual financial framework, became an integral part of the EU budgeting process of mid-term budget planning for the period of no less than five years, which should ensure orderly development of spending within own resources of the EU budget (Art. 312 of the TFEU). Multiannual financial perspectives determine the maximum annual size (ceiling) of budget expenditures subject to areas of use thereof which are limited in number and correspond to major sectors of the Union.

The current multiannual financial perspective for years 2014 – 2020 was identified by total funding of 959,988 million euro at very low average annual growth rate – 101.4%. For this financial period the EU prescribes "doing more – to certain areas – with less losses" as evidence of the low growth rate of financial resources. The bulk of financial resources in this period is directed to preserving natural resources – 38.9%, and economic, social and, regional development – 33.9%. Of the seven major uses of public funds little priority is given to increasing share of expenditure on economy competitiveness and increase of jobs by 3.4%, the measures of EU globalization – 0.4%, administrative expenses – 0.6% and economic, social and regional development – 0.9%, while reducing the share of expenditure on preservation of the environment by 5.5%. The above analysis leads to the conclusion on fairly pragmatic forecasts of the post-crisis united Europe<sup>32</sup>.

An important instrument of influence on the national budget of member countries in terms of adhering to the principle of effective balancing national budgets expenditures with respect to the real income of the same budget includes tools and mechanisms for maintenance and management of public debt, which is

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<sup>31</sup> Financial Regulation and implementing rules applicable to the general budget of the European Communities / Synoptic presentation and selection of legal texts relevant to establishing and implementing the budgets. – European Commission, Luxembourg, Publications Office of the European Union. – 2010. – P.405. – [Electronic resource]. Access mode: [http://ec.europa.eu/budget/library/biblio/.../regulations/syn\\_pub\\_rf\\_modex\\_en.pdf](http://ec.europa.eu/budget/library/biblio/.../regulations/syn_pub_rf_modex_en.pdf) (date of access: 10.10.2014).

<sup>32</sup> European Commission Financial Programming and Budget – [Electronic resource]. Access mode: [http://ec.europa.eu/budget/index\\_en.cfm](http://ec.europa.eu/budget/index_en.cfm) (date of access: 15.10.2014).

almost entirely within the authority of national governments. The main objectives of public debt management includes providing liquidity of the budget and budget system as a whole, as an important regulator of the securities market, where the state becomes its direct participant. Gerd Ehlers, Consultant on finance and budget (Germany) thinks of the public debt management as of the "window on the market" for the state. It should be remembered that the welfare of socio-economic development of any country "due to debt" will inevitably, sooner or later, lead to the collapse of this economy. A striking example of "budgeting on credit" is the economy of Greece, where in 1999 the budget deficit amounted to 3.1% of GNP and was lower among Euro-zone countries – Malta (7.7%), Slovakia (7.4%), Cyprus (4.3%), Estonia (3.5%), and the 2013 debt increased 3.2 times and amounted to 10.0% of GNP, reaching its highest level in 2009 – 15.6%<sup>33</sup>.

Despite citizens' continuous discontent about budget cuts and tax increases, the joint efforts of the EU and the International Monetary Fund of Greece since 2010 have managed to make serious reforms in their public finances. According to Eurostat, last year Greece reached a budget surplus, and at the same time, the debt, which stood at 175% of GNP, may be reduced to 110% only in 2022. However, the slow economic recovery has enabled Greece to return to the capital markets, which may speed up the gradual withdrawal of the economy from deep recession<sup>34</sup>.

Similarly, Malta at the beginning of the 21<sup>st</sup> century has the largest among Euro-zone deficit – 7.7% of GNP, which in 2003 grew by 19.5%. This situation was caused by excessive growth of social benefits in the absence of good GNP growth and simultaneous reduction of the tax burden under the slogan of "business support", which led to increase of public finance deficit in 2003 to 9.2% of GNP. Since 2004 the national government decisions were taken to increase VAT tax at the standard rate from 15% to 18%, measures were taken to increase tax revenue from corporate income, "eco-tax" on environmental pollution was introduced, and others<sup>35</sup> which made it possible to reduce the deficit at the

<sup>33</sup> Euro-zone governments have increasingly broken their self-imposed limit of annual budget deficits of no more than 3% of gross domestic product / THE WALL JOURNAL. Europa. – [Electronic resource]. Access mode: <http://online.wsj.com/.../SB10001424052970203501304577088330321848846> (date of access: 12.10.2014).

<sup>34</sup> EU Confirms Greece Beat Its Budget Targets in 2013. Finance Ministers Could Discuss New Debt Relief Measures as Early as May / THE WALL JOURNAL. Europa. – [Electronic resource]. Access mode: <http://online.wsj.com/.../SB10001424052702304788404579519260485935416> (date of access: 12.10.2014).

<sup>35</sup> *Tulai Constantin, Sabău - Popa Claudia Diana*, (2009) Budgetary Consolidations in EU-12. The annals of the University of Oradea, Economic Sciences, Volumul III – Sectiunea: Finante, Banci si

time of entry into the Euro-zone, from January 01, 2008. For 2012 the deficit was kept at 3.3%. An example of "fiscal paradise" in the history of the EU economy is Cyprus, where the low effectiveness of the consolidation and lack of political will to confront the increase of budget expenditures led to the fact that under the Stability Pact for countries in the period 2004-2006, the EU had been applying the procedure of excessive deficit. Meanwhile, in a turbulent financial market economy of Cyprus still is not able to properly resist competitiveness of tourism business, a deficit trade balance is kept, as well as increased investment demand and other factors that require tight restructuring of public expenditure, and therefore the deficit at the beginning of 2014 continues to be at 6.3% of GNP<sup>36</sup>.

The analysis of public finances in Greece, Cyprus, Spain, Malta and other EU countries is the substantiated proof of the low efficiency of exercise of their powers by national governments on the management of public finances and public debt in particular. It is appropriate to recall that the Maastricht Treaty (Art. 5 of the consolidated version) back in 1992 introduced the principle of subsidiarity, which involves the transfer of national powers, implementation of which is ineffective – the supranational level. Taking into account the situation prevailing in some EU countries in balancing their national budgets, powers on debt planning, servicing, and management are subject to partial centralization and consolidation within powers of the Commission, relevant committee, and Directorate-General for Budget<sup>37</sup>.

The practice of inter-institutional agreements as part of the budget law was introduced in the EU since founding of the Community and is part of regulatory framework that ensures flexible application of primary legislation. The special role of the application of such agreements in the budget process should be noted, where since development of the EU budget system such

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Contabilitate, Tom XVIII 2009 – Volumul III – Sectiunea: Finante, Banci si Contabilitate, p. 415-421. – [Electronic resource]. Access mode: <http://steconomice.uoradea.ro/anale/volume/2009/v3-finances-banks-and-accountancy/69>. (date of access: 09.10.2014).

<sup>36</sup> Provision of deficit and debt data for 2012./ Eurostat news release euro indicators, 64/2013 – 22 April 2013. – [Electronic resource]. Access mode: <http://epp.eurostat.ec.europa.eu/.../2-22042013.../2-22042013-AP-EN.PDF> (date of access: 15.10.2014).

<sup>37</sup> Directorate-General for Budget operates within the Commission, and its primary powers include arrangement of the budgeting process, it is responsible for collection of own receipts of EU budget from member states, it keeps the accounting, including accounts of the Commission, and consolidated accounts of European institutions, and prepares the financial statements. Management of appropriations of the EU budget is not among powers of the Directorate, they are exercised by relevant departments of the Commission. Directorate-General consists of five administrations based in Brussels and counts over 400 employees. – [Electronic resource]. Access mode: [http://ec.europa.eu/dgs/budget/index\\_en.htm](http://ec.europa.eu/dgs/budget/index_en.htm) (date of access: 12.10.2014)

process regulates changes to the division of powers between the relevant institutions. This regulatory mechanism has been applied actively since introduction of the medium-term budget forecasting of EU spending. The first agreement was in 1988, it was between the European Parliament, the Council and the Commission on budgetary discipline and improvement of the budget process in 1988-1992<sup>38</sup>. To ensure the financial perspective of years 2014-2020 adoption of Interinstitutional Agreement on cooperation in budgetary matters and on sound financial management<sup>39</sup> is expected, which provides three main areas:

- 1) additional provisions related to the multiannual financial perspective and specific provisions that are not included in the financial framework;
- 2) cooperation on budgetary procedures;
- 3) provisions for sound financial management of EU funds.

An important role in the budget process in the EU is played by a control over compliance of budget legislation, which is carried out by the relevant institutions of EU and member states. EU Court of Auditors as a separate, independent collegial body of external control (Art. 285-287 of the TFEU), the basis of which is the system control, which stipulates, in contrast to the method of inspection of accounts or contractual obligations, mainly auditing based on accounting information, and in some cases, if necessary, on-site inspections in other institutions of the Union.

The joint budget as the main object of the budget process by its structure corresponds to national budgets which include revenues and expenditures. However, the EU budget is significantly different from the national budget by peculiar budget process, the composition and structure of income and expenditures and being deficit-free. Unlike budgets of other integration associations, budgets which consist of contributions from members of the integration structures, the EU budget is formed by revenues from own revenues of the Union and the proceeds collected in the territories of member states and transferred to the common budget in accordance with EU legislation, and therefore it is inherently the budget of "convergent development of community" and not only the "budget of integration costs", which the budgets

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<sup>38</sup> Interinstitutional Agreement of 29 June 1988 on budgetary discipline and improvement of the budgetary procedure, / Official Journal of the European Communities (OJEC). 15.07. 1988, n° L 185. [s.l.]. – [Electronic resource]. Access mode: [http:// www.cvce.eu/content/publication/1999/1/1/.../publishable\\_en](http://www.cvce.eu/content/publication/1999/1/1/.../publishable_en). (date of access: 14.10.2014).

<sup>39</sup> Draft Interinstitutional Agreement between the European Parliament, the Council and the Commission on cooperation in budgetary matters and on sound financial management /European Commission. – [Electronic resource]. Access mode: [http:// www.cvce.eu/content/publication/1999/1/1/.../publishable\\_en](http://www.cvce.eu/content/publication/1999/1/1/.../publishable_en). (date of access: 14.10.2014).

of other integration associations are. Nevertheless, the EU budget, equally as other integration budgets, the remains the "pooling" budget where perennial controversy — how much who pays and how much who gets — remains relevant forever.

According to the EU draft budget for 2015 its revenue, and therefore the total amount is assumed at 142.1 billion Euros, 1.9 billion Euros more than the budget approved for 2014.

The Council identified three types of own resources of the EU budget:

- traditional own resources generated from the proceeds of duties and fees, which since 2014 are transferred to the budget by the Member States at 20% the amount determined payable, instead of 25% as was previously established;
- own resources in the form of deductions from the VAT resource at a rate of 0.3%;
- own resources in the form of contributions from member countries of the GNI resource used solely as a mechanism for determining the amount of contributions and is paid on a monthly basis on the amount specified in the EU budget for the current budget period, at the expense of national budgets.

Thus, all the EU budget revenue, in addition to other income are considered to be own revenues based on the EU methodology. However, in its essence, revenues transferred to the joint budget with the consent of member states are nothing like their contributions, determination and payment of which is dependent on the harmonized bases of deductions — VAT and GNI.

In the revenue structure of the EU budget s of its volume is occupied by contributions member states from GNI resource, which, in our view, is nothing but a transfer (most likely grant or contribution of member states) to balance the deficit-free budget of the Union, which is why inclusion of this type of income to own resources, and not entirely transparent and parity mechanisms for its correction, rightly cause discontent from some of the major donors to the EU budget (UK, Germany, France etc.), members of the European Parliament on reformation of the EU budget and seeking new sources of income. One of the main problems restraining the expansion of financial impact of the EU budget expenditures to the level of convergence of socio-economic development of member countries and the changes occurring in the global financial system is still extremely high level of transferness of the EU budget (87%) where income from such "transfers" is fully dependent on the unanimous agreement of member

countries and is the direct removal from their national income.

Of course, creators and administrators of the EU budget are constantly thinking about increasing its volume because there is an annual need for funds to finance regional issues: research, education, environmental protection, migration and employment, uneven socio-economic development of a large part of the EU and others. One of the areas to increase their own revenues could be a tax on the transaction which, according to the Commission estimates, can generate 30-35 billion Euros of revenues<sup>40</sup>.

Analysis of integration development of budgetary relationships gives reason to conclude that the priority of a common fiscal policy was and still is public spending policy, which is implemented through the use of the following mechanisms: cost allocation according to needs; compensation of costs due to the operation of the common market; votes compromise when making decisions on allocation of the budget. The lack of scientific and reasonable distribution system, and therefore the definition of realistic expenditure fixed in the basic law of the EU and not in treaties, lead to the fact that the EU budget has become a kind of "trading platform" where, as noted by S. Hix, a scientist from the UK, a game is played in which each state pays/receives from the EU budget as much as they receive/lose from the extra-budgetary policy of the EU<sup>41</sup>.

For a long time the main item of budget expenditures was expenses on maintenance and development of agriculture, which until the late 1980s of the last century made up the bulk of the expenditure budget despite the fact that the share of agricultural products held within 2% of the EU GDP<sup>42</sup>. Reforms implemented in the EU significantly changed and stabilized the structure of joint budget expenditures (Table 1).

For the 2014-2020 period priority of economic policy is to strengthen the impact of financial instruments on sustainable development and economic growth by increasing the level of employment, for which over the next seven years, despite 3.44%

<sup>40</sup> How the EU budget is financed The "own resources" system and the debate on its reform. – EPRS | European Parliamentary Research Service Author: Alessandro D'Alfonso Members' Research Service June 2014. – [Electronic resource]. Access mode: <http://www.europarl.europa.eu/thinktank/en/document.html?reference=LDM...> (date of access: 29.10.2014).

<sup>41</sup> Hix S. The Political System of the European Union / S. Hix // The European Series. – Palgrave Macmillan. – 1999. – [Electronic resource]. Access mode: <http://www.lse.ac.uk/researchandexpertise/experts/profile.aspx?...s.hix%40lse...> (date of access: 29.10.2014).

<sup>42</sup> Alesina A., Giavazzi F. The Future of Europe: Reform or Decline [Electronic resource]. Access mode: [http://books.google.com/books/about/The\\_Future\\_of\\_Europe.html?id...](http://books.google.com/books/about/The_Future_of_Europe.html?id...) (date of access: 29.10.2014).

(34.2 billion Euros) reduction in the total volume of budget appropriations, compared to 2007-2013, increase of spending is stipulated by 34.1 billion Euros or 3.88%. The equally important factor of growth and stability will also be strengthening the regional component of EU policy, covering economic, social, and regional cohesion by helping to overcome the backlog of individual countries and regions of the EU to strengthen competitiveness and regional cooperation, the share of expenditure on which in their total structure will grow by 1.87%, while the volume of appropriations for this goal will be reduced by 30.1 billion Euros. Thus, the component of costs on sustainable economic growth, with almost constant volume of allocations from the budget (+4 billion Euros), is scheduled to increase by 2.02%.

Table 1

**EXPENDITURE STRUCTURE OF THE EU BUDGET IN ACCORDANCE WITH  
FRAMEWORK FINANCIAL PERSPECTIVES OF YEARS 2007 – 2013 AND 2014  
– 2020 (IN EURO BILLIONS AND %%)<sup>43</sup>**

	2007 – 2013		2014 – 2020		+/- in% 2014- 2020 to 2007 – 2013
	Amount	%	Amount	%	
1. Sustainable development and growth	446,8	44,94	450,8	46,96	+2,02
1a. Competitiveness for higher employment rate	91,5	9,20	125,6	13,08	+3,88
2b. Economic, social, and territorial development	355,3	35,73	325,2	33,86	+1,87
2. Natural resources preservation and management, including: market and direct payments	420,7 318,8	42,32 32,07	373,2 277,8	38,88 28,94	-3,44 -3,13
3. Citizenship, freedom, safety, and justice	12,4	1,25	15,7	1,63	+0,38
4. EU as the world partner	56,8	5,71	58,7	6,11	+0,40
5. Administrative costs	56,5	5,68	61,6	6,42	+0,74
6. Compensations	1,0	0,10	—	—	-0,10

<sup>43</sup> Compiled by authors based on data of:

— European Commission The Multiannual Financial Framework 2014-2020 – Frequently Asked Questions. – [Electronic resource]. Access mode: [http://ec.europa.eu/budget/mff/index\\_en.cfm](http://ec.europa.eu/budget/mff/index_en.cfm) (date of access: 30.10.2014);

— Council European of the European Union, Brussels, 27 June 2013. – Draft Council Regulation laying down multiannual financial framework for the years 2014-2020. – [Electronic resource]. Access mode: <http://www.consilium.europa.eu/media/2060418/st11655.en13.pdf> (date of access: 31.10.2014).

Total allocations for undertaking	994,2	100	960,0	100	-3,44
in%% to GNP	1,12	x	1,00	x	-0,12
including allocations for payments – total	943,1	94,86	908,4	94,63	-0,23
in%% to GNP	1,07	x	0,95	x	-0,12

The United Kingdom has the highest level of negative balance of intergovernmental relations, where despite the adjustment applied to contributions to the EU budget, it received appropriations for more than a third (36.87%) of contributions it paid to the EU budget, as well as Hungary – 5.8 times more than it put into the budget. Dynamics and projected mathematical calculations made by the authors with respect to budgetary relations in the EU by 2020 confirm that the current policy of cohesion of spending powers does not encourage the need to increase the rate of return of national economies of recipient countries, at the same time, despite the strength of the economies of donor countries, growth rates of contributions to the EU budget it has a negative impact on their socio-economic status and political balance of partnership relations.

Overall, the EU budget system, both at the supranational and national levels requires substantial reform, which is to apply more flexible financial instruments of budgeting, models and forms of economic relations between the EU institutions and member states to strengthen the efficiency of the EU Anti-Fraud Office, to improve the system of supranational control, and others. However, in the EU budgeting an important role is played by combination of vertical convergence of EU budget expenditure with the horizontal convergence, which is vastly applied in the EU tax policy – the harmonization and unification of tax systems of member countries.

### Conclusion

Based on many theoretical and analytical studies of Ukrainian and foreign scientists, scientific developments of relevant EU institutions and academic institutions, as well as our own economic and mathematical calculations of processes of consolidation in the EU budgetary process, and analysis of institutional interactions between actors of this process we made the following conclusions:

1. In the evolution of regional economic integration in conditions of growing globalization of the world financial system, which is in a dynamic development of information and communication technologies, the impact of budget and discretionary meas-



which is in a dynamic development of information and communication technologies, the impact of budget and discretionary measures on the condition of financial resources of the regional and world economy is increasing. The analysis shows that during the recession, most countries have resorted to increased discretionary measures excluding their main instrument of macroeconomic balance of financial resources (deficit and public debt) of national budgets without changing the policy of ever-increasing budget expenditures, indicating a slow pace of fiscal consolidation. Measures to reduce spending of the EU budget for financial perspective of 2014-2020 and strengthening of fiscal pressure used before (tax increase) by 2017 will enable reduction of the budget deficit, subject to a significant increase in the efficiency of budget spending. However, given the political and economic limitations of fiscal pressure, in the next three years the tough fiscal consolidation policy of the EU, in our opinion, should gradually change to policy of tax easing, as a factor stimulating the economy, while maintaining tight expenditure consolidation.

2. Political differences over the fair participation of member states in budgeting and other budgetary and financial matters of joint EU activities require new approaches to scientific and theoretical study and use of the classification structure of budget revenues. There is no doubt about traditional revenues, which by their nature are own revenues. However, the deduction from VAT and GNI resource does not perform the functions of their own revenues, and are contributions of the member states, as evidenced by the constant change of priorities of their receipt and adjustment in favor of individual countries. Proposals to introduce new revenue of the joint budget may be perspective, while levying such revenue would minimize the fiscal burden on the economies of member states. Such revenue may include taxes (charges) related to activities of the EU institutions, including monetary and international activities.

3. The global financial crisis of 2007-2009 forced EU institutions and governments of member states to take more effective measures to reduce regional imbalances of public funds, compliance with the criteria set by the Maastricht Treaty, ratios of public debt and deficit of national budgets of member states. The imbalance of public debt and borrowing in a number of countries increased effects of the financial crisis and due to political disagreement they led to application of restrictions by the EU. The Maastricht criteria are increasingly violated not only by recipient countries, but also by donor countries that, to a certain extent,

gives rise to doubt about the effectiveness of introduced mechanisms of restrictions. The high level of budget deficit and debt load of national budgets requires taking coordinated measures of fiscal and monetary policy which requires clear clarity on the real relationships of macro-financial indicators that can be ensured not always, and not in all countries by relation of these indicators to the GDP (GNP) due to its probable inaccuracy. It would be advisable to hold special scientific and practical research on the use of the mechanism of regulation of national budgets debt load to their volume in relation to the level of the fiscal burden per capita.

4. The EU ability to confront challenges of globalization will depend on the priorities and expenditure structure of common budget. It is impossible to disagree with a number of proposals to increase spending on research, education, labor markets, increase of competitiveness, creation of necessary conditions for respecting the rights, freedoms and social protection of citizens as fundamental values of the Union. Priority requirements for the EU budget spending policy is substantially higher efficiency of common budget which draws attention of politicians, scholars, and representatives of NGOs. In particular, expenditure funding from the EU budget through non-governmental organizations and civil society is not transparent and is not sufficiently substantiated. In general, activity of the EU budget, given the current imbalances in inter-budget relations requires the development of new, more effective mechanisms of institutional management of common budget and strengthening of fiscal consolidation of the EU and member states of this basis.

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