



# EU News

## Monthly Journal

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Dear readers,

The European Union came to a crossroads this June. The last summit of the European Council on 16 and 17 June, on the occasion of the end of the Luxembourg presidency, failed to arrive at an agreement about the budget for 2007-2013. This crossroads is a good opportunity to have a period of – as officially called – reflection. Reflection on where the European Union has got to and especially where it should develop in the future.

We warned here in the Editorial last month that the Constitution ratification process could paralyze the ability to agree on a budget. And that is exactly what happened. Debate over the budget for 2007-2013 involved several tiers of discussions and different approaches. One tier concerned the total volume of funds that should be redistributed through the EU budget. Rich countries, logically from their point of view, required that the volume be as small as possible. On the other hand, the countries that could expect to draw on the budget outlay most required an increase of the percentage. Another tier in the argument concerned the sum each country may receive in the form of Structural Funds during a year. In the end, however, the clash between 'rich' and 'poor' ceased and the 'poor' were willing to make considerable concessions, knowing that in spite of the concessions their position in drawing on the European funds would be much better than now. And also that the sooner the negotiation ends, the more time they will have to prepare new, good Operational Programmes through which they will be able to realistically improve their absorption ability to draw on the European funds.

But there was actually more and more rivalry in the group of the rich, which could be simplistically symbolized by a clash between France and the UK. France would have liked to defend the traditional orientation of the European funds. The UK approach preferred a significant drop in agricultural expenditures and, in accordance with the New Lisbon Agenda, making the EU aid policy take much greater account of the factors in which the EU as a whole could compete with other 'rivals' in global competition – a higher share of expenditures on science, research, education, improvement of the entrepreneurial environment, hand in hand with further deregulation of the single internal market.

The current period of reflection should provide an answer to the emerging questions. We can say that European integration has experienced various hiccups in the fifty years of its history. The more members the grouping has, the more complicated these hiccups are. However, we should probably reserve such terms as crisis, fiasco or the worst period in the history for a situation that will truly correspond to the seriousness of the words.

Summer is quite a favourable period to give at least some of the answers. Enjoy the summer with European topics in the company of our EU News Monthly.

Petr Zahradník



## Events

The European Council has not brought much optimism. In spite of demanding and lengthy negotiations, member state leaders have not reached an agreement about the EU's future financial framework for 2007-2013. One stumbling block was a request to cancel the 'UK rebate', which British Prime Minister Tony Blair was willing to give up only if the importance of the common agricultural policy diminished. The United Kingdom is the EU presiding country in the second half of this year, and its priorities include a common Union budget reform.

### POLITICS

#### Priorities of the UK presidency of the EU

The United Kingdom takes the helm of European Union bodies for the second half of this year. In an address to the European Parliament at the end of June, Prime Minister Tony Blair outlined the priorities of the UK presidency, which will focus on market-oriented economic reforms, debate about the future of Europe and common budget restructuring.

Mr Blair also denied the accusations of certain European politicians, in particular Luxembourg Prime Minister Jean-Claude Juncker, that his only interest was converting the EU just to a free trade zone and declared himself a keen pro-European. The main points of Mr Blair's address:

**European budget** – The United Kingdom is willing to give up its rebate on contribution to the common European budget negotiated by Margaret Thatcher in 1984 only if expenditure on the common agricultural policy drops. This change may happen in the second half of the budget period of 2007 to 2013. On the other hand, expenditures on science, research and education should increase.

**Ratification of the Constitution** – According to Blair, the rejection in France and the Netherlands was not due to its wording but to the citizens' deeper dissatisfaction with the European Union. It would now be difficult for most member states to ensure a majority of YES votes. Politicians should therefore listen to the citizens more and deal with their needs.

**Economic reforms** – a UK presidency would like to improve European economic regulation, which should not be a burden for business and job creation, and finish the Services Directive, which would open this largest economic sector to cross-border competition. However, economic growth should not be at the expense of future generations; the United Kingdom supports a sustainable development concept. The next half year should also see radical progress in adopting the chemicals registration legislation, REACH, and the remaining legislation under the Action Plan for Financial Services.

**Social Europe** – Mr Blair advocates a strong social dimension, he would not accept the European project as a purely economic market. However, the goal of the social model should increase the ability to compete internationally, cope with the globalisation process, allow people to seize opportunities and overcome fear. The reform should allow the social model to truly work.

**External relations** – The USA is the only work superpower. But China and India will be the world's largest economies in a couple of decades, each with three times the number of residents of the entire EU. The idea of a unified Europe is

therefore important to make the member states strong enough to maintain their importance in the world. That is also why it is necessary to reform all European institutions. Further enlargement of the EU is also desirable from this point of view.

**Other priorities** – Fighting global poverty and aid to African nations, starting work on the global warming control strategy after 2012, progress within the Qatar round of WTO negotiations, asserting peace, stability and reforms in the Middle East, implementing a liberal sugar reform in the EU, developing partnership with Russia and the Ukraine, and a war on global terrorism.

<http://www.eu2005.gov.uk>

#### Constitution ratification will take more time

At the Brussels summit, member state leaders decided to postpone the deadline for European Constitution ratification from the originally determined November 2006 to an unspecified time. Thus the ratification will not stop in principle, but some time is needed for reflection and discussion with citizens after the negative vote of the French and Dutch voters in the recent referenda. The results of the discussion with citizens should be evaluated by the regular EU summit meeting next June, which will decide on the further procedure. The European Council also stated that re-opening negotiations about the Constitutional Treaty is out of the question.

In relation to the European Council's decision, the prepared referendum on the Treaty establishing a Constitution for Europe was deferred in Denmark (the original date was 27/9/2005). The United Kingdom, which considered the next summer, made a similar decision before the European Council. Poland is also deferring ratification with a referendum, which was to take place this autumn, and Prime Minister Belka pleads for ratification by the Parliament. Referenda were also postponed in Ireland and Portugal. On the other hand, swimming against the tide in order to prove the Constitution's viability is Luxembourg, which confirmed the date of 10 July; in addition, Prime Minister Jean-Claude Juncker has made its result a condition for his continuance in office.

No date has been agreed in the Czech Republic. Coalition parties wanted to combine it with the parliamentary election in June 2006; the opposition ODS wanted a referendum as early as by the end of this year. According to Prime Minister Jiri Paroubek, the most probable date is now the end of 2006 and beginning of 2007.

The Treaty has been approved by ten countries so far, two have rejected it. However, the Constitution will only come into effect if it has been ratified by all 25 members without exception. Theoretically, it is possible to have the voting

process repeated in France or the Netherlands, as happened in Ireland (with the ratification of the Treaty of Nice) and Denmark (with the ratification of the Maastricht Treaty), and hope that they will say YES this time. However, this is not very probable, as in these countries the Constitution was rejected by a clear majority of the vote and as a whole – not only because of some controversial parts of the text. The possibility cannot be excluded that in the end the Constitution will only be approved in a reduced form which would focus mainly on modernizing the decision-making mechanisms.

<http://www.eu2005.lu/en/actualites/conseil/2005/06/17conseil-decl/index.html>

### Ratification of the European Constitution

Member State	Procedure	Date scheduled
Austria	Parliamentary	Approved: 25.5.2005
Belgium	Parliamentary	July 2005
Cyprus	Parliamentary	Approved: 30.6.2005
CR	Referendum	probably the end of 2006-beginning of 2007
Denmark	Referendum	Postponed (previously scheduled on 27.9.2005)
Estonia	Parliamentary	Autumn 2005
Finland	Parliamentary	the end of 2005 or the beginning of 2006
France	Referendum	Rejected: 29.5.2005
Germany	Parliamentary	Approved: 27.5.2005
Greece	Parliamentary	Approved: 19.4.2005
Hungary	Parliamentary	Approved: 20.12.2004
Ireland	Parliamentary + Referendum	Postponed
Italy	Parliamentary	Approved: 6.4.2005
Latvia	Parliamentary	Approved: 2.6.2005
Lithuania	Parliamentary	Approved: 11.11.2004
Luxembourg	Parliamentary + referendum	Approved: 10.7.2005
Malta	Parliamentary	Approved: 6.7.2005
Netherlands	Parliamentary + referendum	Rejected: 1.6.2005
Poland	Referendum	Postponed (previously scheduled on 9.10.2005)
Portugal	Referendum	Postponed (previously scheduled on October05)
Slovakia	Parliamentary	Approved: 11.5.2005
Slovenia	Parliamentary	Approved: 1.2. 2005
Spain	Parliamentary + referendum	Approved: 18.5.2005
Sweden	Parliamentary	Postponed (previously scheduled on December05)
UK	Parliamentary + referendum	Suspended

Source: European Commission

## BUDGET

### Member states fail to agree on an EU budget

The European Council ended with a failure, as the leaders of the twenty-five EU member states failed to agree on a compromise form of the European Union's financial perspective for 2007 to 2017.

The failure of negotiations was caused mainly by the stubbornness of the United Kingdom and France. UK Prime Minister Tony Blair made giving up the UK 'rebate' on the contribution to the common budget conditioned by an overall budget reform and in particular by restricting the high expenditure on the common agricultural policy. However, this was sharply refused by French president Jacques Chirac, whose country is the one profiting most from the common agricultural policy.

Budget negotiations were based on Luxembourg's proposal presented on the eve of the summit meeting. It expected expenditure ('payment appropriations') amounting to 1.0% of the EU's gross national income (GNI) (1.06% for commitment appropriations), as opposed to the 1.14% of the GNI originally proposed by the European Commission. It also expected to preserve regional aid for Spain and southern Italy. Relief was planned for the Netherlands, Sweden and Germany, which are among the countries contributing the most to the common European budget in terms of payment per citizen. In addition, it envisaged freezing the UK rebate at the current level of 4.6 billion euros a year, which was unacceptable for the Britons. Mr Blair conditioned concessions in the UK rebate by diminishing the importance of agriculture.

Presiding Luxembourg therefore proposed during the negotiations to incorporate three-quarters of the agricultural subsidies for Bulgaria and Romania from 2007 in the bundle the EU had agreed upon in 2002 but only for 25 countries. As for the UK, Luxembourg Prime Minister Jean-Claude Juncker proposed increasing the frozen UK rebate to 6.2 billion euros a year, but this did not pass either. The new member states were not required to finance it. In addition, the approved budget included a commitment to review EU financing from 2009 based on the Commission's proposals.

The new members realized that if the financial perspective was not approved and there was a delay in its acceptance, it would be mainly they who would be affected negatively, as they get a major part of the contributions from the EU under regional policy. That, however, is strictly tied and late budget approval may result in delays in the preparation of programmes and then projects, which may prevent using up all of the funds. Therefore, representatives of the Visegrad



## Events

Group countries supported by Latvia and Lithuania were willing to give up a part of the regional policy contributions in order to allow adopting a compromise. Poland's Prime Minister Marek Belka is even reported to have asked directly 'if it's a question of money, how much do you want?' But even that didn't help.

In the end, the modified Luxembourg proposal was opposed not only by the UK but also by the Netherlands, Sweden, Spain and Finland. The remaining 20 countries voted for it, but a financial perspective must be adopted unanimously.

From a momentary point of view, the failure to approve a budget framework for the EU seems to be a serious political crisis. However, if it results in a true reform of the European budget that re-assesses budget priorities in favour of increasing the expenditures on science, research, innovation, job creation at the cost of agriculture and that fully reflects the Lisbon strategy, it will be a clearly positive milestone in the history of European integration. During the next half a year, the European Union will be presided by the United Kingdom, which would like to follow through with this vision successfully. However, its position will be very difficult as Tony Blair has made a lot of enemies due to his stubbornness, especially in France and Luxembourg. It is therefore more probable that no compromise will be approved until Austria's presidency in the first half of 2006.

The prolongation of the financial framework approval process is unpleasant but not tragic. For instance, the current financial perspective for 2000 to 2006 was adopted in the spring of 1999. If the prepared budget is also approved nine months before it takes effect, it may still be possible to adopt the necessary implementation legislation as well as to prepare national documents for using the money.

<http://www.eu2005.lu/en/actualites/communiqués/2005/06/17jcl-pf/index.html>

<http://www.europa.eu.int/rapid/pressReleasesAction.do?reference=DOC/05/2>

## FOREIGN TRADE

### EU and China agree about textile

China will restrict the growth in clothing and textile exports to the European Union in ten different product categories to 8% to 12.5% annually, with effect from 20 June. This is the result of an agreement that has terminated the dispute between the EU and the Asian giant concerning a dramatic increase in Chinese textile imports to Europe after the import quotas were released this January. For instance, t-shirt imports grew by 187% in comparison with the last year.

The trade war between China and the European Union has been warded off – after negotiations, the biggest country in the world - China - will voluntarily limit its textile exports to the Union, which has been smothering European textile mills. The European Parliament and the Council have agreed on a directive requiring the registration of cash transported across the EU external borders.

According to the Commission, the agreement should control Chinese textile exports by the end of 2008. Its conclusion warded off the imposition of import quotas by the EU, to which the EU was entitled according to the rules of the WTO. The agreement still must be approved by the EU states to enter into force. China is striving to reach a similar agreement with the USA, whose textile industry is also suffering from floods of cheap Asian competitor products.

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=MEMO/05/201>

## INTERNAL MARKET

### The movement of cash totalling more than EUR 10,000 will be registered

The European Parliament and the EU Council agreed on a compromise text of the regulation concerning the control of cash movement to and from the European Union. It should enter into force within 18 months after publication in the Official Journal, i.e. mid-2007.

The goal of the regulation is to help the fight against money laundering and funding terrorism. It introduces harmonized border control of cash movement and strengthens cooperation between competent authorities. It imposes an obligation to notify the authorities of cash movement across the EU's external borders if the amount exceeds EUR 10,000 (or the equivalent amount in another currency or easily convertible assets such as traveller's cheques). Responsible member states are obliged to introduce appropriate punishments for people taking cash across the external EU borders without notification.

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/702>

### The Commission will look into retail banking and enterprise insurance

The European Commission is going to perform an in-depth inspection in the retail banking and enterprise insurance sectors in order to discover any possible agreements, decisions or practices leading to breaches of competition rules. The Commission's investigation is complementary to the initiative of the Commissioner Charlie McCreevy, for the creation of a single financial services market.

According to the Commission, there is certain evidence suggesting restriction on competition in the market: price differences for comparable products, diversity of European bank profitability, division of the market by large banks in some countries or a lack of cross-border bank fusions and acquisitions.



The in-depth investigation will start in retail banking and focus mainly on the differences in fees charged for cross-border use of debit and credit cards. Investigation into enterprise insurance will follow. A report with the results will be published next year. The commission has authorization to take firm action in the event of a breach of competition rules, either on its own or through the individual national competition authorities.

The financial sector has been chosen due to its economic importance rather than frequent occurrence of problems restricting the competitive environment. Yet the result of the investigation may have a huge impact on the future regulation of financial markets, striving for as much integration as possible.

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/719>

## Savings Tax Directive enters into force

On 1 July, the controversial directive on the taxation of interest income from savings enters into force. The objective of the directive is to allow putting a tax on savings interest earned in a third member state according to the home member state's legislation, thus removing barriers in the free movement of capital in the single market.

The basis of the directive is a mechanism through which banks will notify tax authorities in other member states of the interest income of their citizens. Belgium, Luxembourg and Austria will not participate in the system, being granted a transitional period during which they have to apply a withholding tax on savings interest instead of sharing information with other member states. The tax is set at 15% for the first three years of the transitional period, 20% during the next three years and 35% during the last three years. They will anonymously transfer three-quarters of the tax revenue to the account owner's tax authority. The new directive will only apply to individuals and their accounts.

For the directive to come into effect, the tax shelters of Switzerland, Lichtenstein, Monaco, Andorra and San Marino had to join it through international treaties. These countries will apply the same income anonymity exemption as the three member states above.

[http://europa.eu.int/comm/taxation\\_customs/taxation/personal\\_tax/savings\\_tax/index\\_en.htm](http://europa.eu.int/comm/taxation_customs/taxation/personal_tax/savings_tax/index_en.htm)

## EMPLOYMENT AND SOCIAL POLICY

### Ministers fail to agree on Working Time

Member states' ministers of labour and social affairs have failed to agree on the European Commission's proposal to

remove the opt-out clause from the Working Time Directive after 2012.

The draft Working Time Directive amendment discussed by the ministers was an attempt at a compromise, as the European Parliament voted to scrap altogether the controversial opt-out that allowed employees to work more than 48 hours a week by their own request. MEPs are inclined to worry about the abuse of the 'voluntary' request due to employer pressure. The European Commission chose a middle path that envisaged continuing the opt-out for three years after the implementation of the approved Directive, i.e. until 2012. Member states could then request an extension from the Commission, but only for 'reasons relating to their labour market arrangements'. However, employees would not be allowed to work more than for 55 hours a week in countries keeping the opt-out.

This, however, was not acceptable to the United Kingdom, Slovakia or the Netherlands, which warned of the restriction of competitiveness if the opt-out were cancelled. Current legislation that allows the opt-out will remain in place and the matter is likely to carry on into 2006.

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=MEMO/05/187>

## ENTERPRISE

### The Commission presents a state aid policy reform

The European Commission wants to simplify the rules for state aid and orient it more towards the implementation of the Lisbon Strategy.

An integral state aid policy reform for the next five years was presented as an action plan in early June. The action plan foresees a period of three months for public comments.

The main objective of the reform is to ensure that government spend less money on aid provided to industries with little or no future and focus more on sectors able to generate more economic growth, job opportunities and social cohesion. With its initiative, the Commission wants to make member states provide more support for innovation, research and development, environmental efficiency, or to help less developed regions.

State aid-granting rules should be more transparent and less bureaucratic. The European executive is considering enlarging the block of exemptions in training, employment, research and development, regional development and the environment.

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/680>

## Events

The European Commissioner for Agriculture, Mariann Fischer Boel published a proposal for a far-reaching sugar financing reform under the common agricultural policy, which should cut its prices by almost two-thirds within two years. The European Commission presented a negotiating framework for Turkey's accession to the European Union, which is the most rigorous in the entire history of EU enlargement.

### ENERGY AND TRANSPORT

#### MEPs support energy savings

A controversial draft directive requiring savings in households and in the public sector has found support in the European Parliament. The directive aims at cutting CO2 emissions dramatically. The proposed directive for energy end-use efficiency and energy services was tabled by the European Commission as part of its energy package in December 2003. The directive targets both the demand and the supply sides by creating incentives for reduction and covers electricity, fuel and heating.



In the first reading, the European Parliament backed mandatory targets for savings in energy sold and distributed to households and the public sector. MEPs have voted for more ambitious targets than those initially planned by the Commission, proposing that a total of 11.5% savings be achieved between 2006 and 2015 (the Commission had proposed 1% per year, i.e. a total of 9%). MEPs have even demanded a total of 16% savings in the public sector. The methods of achieving these goals should include energy audits, EPC and energy services also offered by energy companies. The European Parliament also backed the recommendation that energy savings be taken into consideration in public tenders.

The draft directive is to be adopted by the 'co-decision procedure', it must be approved by the European Parliament and the EU Council. However, member states' ministers request that the ambitious savings targets be non-binding and not subject to sanctions. The proposal was also rejected by Deputy Minister of Industry and Trade Martin Pecina, representing the Czech Republic, as we can expect a growth in the absolute energy consumption rather than a drop while catching up with the more developed member states.

Nonetheless, the Commissioner for Energy, Andris Piebalgs, insists on binding targets without which the directive would have no bite and believes that a compromise will be adopted.

[http://www2.europarl.eu.int/omk/sipade2?SAME\\_LEVEL=1&LEVEL=3&NAV=X&DETAIL=&PUBREF=-//EP//TEXT+PRESS+DN-20050607-1+0+DOC+XML+V0//EN#SECTION4](http://www2.europarl.eu.int/omk/sipade2?SAME_LEVEL=1&LEVEL=3&NAV=X&DETAIL=&PUBREF=-//EP//TEXT+PRESS+DN-20050607-1+0+DOC+XML+V0//EN#SECTION4)

### AGRICULTURE

#### The EU reforms the sugar market

The European Commissioner for Agriculture, Mariann Fischer Boel, has published a proposal for a radical sugar funding reform within the EU's common agricultural policy. The core of her proposal is reducing the minimum prices of sugar and sugar beet and cutting production quotas to strengthen competition. Over two years (2006-2007), the guaranteed prices of sugar should drop by 39% and the purchase price of sugar beet should be cut by 42.6%. Farmers will only receive compensation up to 60%, incorporated in the single farm payment. They will also be helped by a special restructuring fund during the first four years.

Sugar prices in the EU are now three times higher than world prices. When the reform has been approved, sugar production should drop by up to 6.2 million tons over several years from today's 19 million tons. It will also result in the cultivation of sugar beet only in those countries where it is cost-effective.

The Commission's proposal will be discussed by the EU Agriculture Ministers. The agreement should be made in November and enter into force in next July, says the ČTK.

The proposal is acceptable for Czech farmers, as it does not cut Czech quotas and therefore will not affect production in the Czech market. It will impact most former European colonies in Africa, the Pacific and the Caribbean, which depend on the exports of expensive sugar to the EU.

The EU was also urged to plan this radical reform by a recent decision of the WTO that upheld complaints about the subsidized exports of European sugar from Brazil, Thailand and other countries.

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/776>

### ENLARGEMENT

#### Negotiations with Turkey will be tough

The European Commission presented a negotiating framework for Turkey's accession to the European Union, which is the most rigorous in the entire history of EU

enlargement. The negotiation process is open-ended and the option of a 'privileged partnership' with Ankara remains on the table.

The decision about the initiation of negotiations with Turkey was made at a European Council in last December and confirmed by the recent EU summit in Brussels. The negotiating framework presented by the Commission will have to be approved unanimously by all EU member states at an Intergovernmental Conference on 3 October. If the member states concur, the formal accession talks will formally start the same day.

The EU has set two major conditions for Turkey to meet in order to engage in accession talks: Ankara has to bring into force six outstanding items of legislation (which it did in early June) and sign the protocol extending the Ankara Agreement to the ten new EU states (which is due during the summer). Of course, Turkey has to meet the 'Copenhagen criteria': stability of institutions, existence of a functioning market economy and the ability to take on the obligations of membership.

The pace of the negotiations will depend on Turkey's ability to meet the requirements. The process will be monitored regularly by the European Commission, reviewed by the Council, and will not be concluded before 2014.

In the case of a serious and persistent breach in Turkey of the principles of liberty, democracy, respect for human rights and fundamental freedoms and the rule of law, the Union can push an 'emergency brake' and suspend negotiations. The decision will rest with the Council.

There will be 35 chapters under discussion, in which the EU may request long transitional periods, derogations, specific arrangements or permanent safeguard clauses especially in areas such as the freedom of movement of persons, structural policies or agriculture. Turkey will be obliged to adopt the euro.

Whether accession negotiations with Turkey actually start will depend on the will of member states, of which each has the power to veto them. Turkey's accession is rather unpopular in France and Austria. On the other hand, one of Ankara's supporters is the United Kingdom, which will preside the Union in the second half of this year.

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/807>

## JUSTICE AND HOME AFFAIRS

### Will controls at EU borders end in 2007?

This June, which sees the 20<sup>th</sup> anniversary of the signing of the Schengen agreement concerning the free movement of

persons across internal EU borders, the Commission published a proposal to extend the borderless zone to the new EU member states and Switzerland with effect in 2007.

A necessary precondition for the extension is including the member states in the prepared Schengen information system (SIS II), which will replace the current system with insufficient capacities and should be put into operation in the spring of 2007. It is a database that tracks stolen vehicles, goods, firearms and missing persons and is also an integral part of the EU's law enforcement strategy.

The new system contains biometric data and will be used to store and disseminate information on extradition, about persons refused entry to an EU country and individuals subject to an international arrest warrant. Control at the external borders is strengthened simultaneously.

The borderless Schengen area now consists of fifteen countries: the original EU-15 members save the United Kingdom and Ireland plus Norway and Iceland.

As soon as the Czech Republic becomes part of the Schengen area, there will be no controls at all when travelling to neighbouring countries. 'There is every reason to believe that Czech nationals will be able to travel without controls at our borders as early as the second half of 2007,' said Interior Minister Frantisek Bublan to the Czech News Agency (ČTK).

<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/651>

### Parliament against data retention

The European Parliament (EP) has rejected the EU Council's justice and home affairs initiative to store all data resulting from phone and online communication for a period of three years. The reason was doubts on the legal basis and the proportionality of the measures that were intended to help fight serious crime, including terrorism. Members of the EP demand that member states produce a study proving the unquestionable need for the proposed arrangements.

Luxembourg minister Nicolas Schmit, the acting president of the EU in this half a year, said that in spite of the rejection in the Parliament, the Council would stick to its original proposal. In such a case however, Alexander Alvaro, a MEP from Germany, is going to lodge an appeal with the European Court of Justice. Commissioner for Justice and Home Affairs Franco Frattini announced that the European Commission would present a new proposal by this summer, which would rest on a different legal basis.

<http://www2.europarl.eu.int/omk/sipade2?PUBREF=-//EP//NONSGML+REPORT+A6-2005-0174+0+DOC+WORD+V0//EN&L=EN&LEVEL=3&NAV=S&LSTDOC=Y>





# Diary

Among events that did not make it to the commented 'Events' section, one worth mentioning is the European Parliament's draft financial framework for 2007-2013, which however has a slim chance of passing. Attention should also be paid to the European Commission's activities in dealing with the excessive deficit of public budgets in Italy and Portugal, which should be subject to the already modified, more flexible and softer rules of the Stability and Growth Pact.

## 01 JUNE

7th Euro-Mediterranean Conference of Ministers of Foreign Affairs, Luxembourg, 30-31.05.2005 (Agreed conclusions): [http://ue.eu.int/ueDocs/cms\\_Data/docs/pressData/en/er/85023.pdf](http://ue.eu.int/ueDocs/cms_Data/docs/pressData/en/er/85023.pdf)

Economic and Financial Affairs: Public finances in EMU: [http://www.europa.eu.int/comm/economy\\_finance/publications/european\\_economy/public\\_finances2005\\_en.htm](http://www.europa.eu.int/comm/economy_finance/publications/european_economy/public_finances2005_en.htm)

Employment, Social Affairs & Equal Opportunities: 2007 to be "European Year of Equal Opportunities for All": [http://www.europa.eu.int/comm/employment\\_social/news/2005/jun/antidiscrimination\\_en.html](http://www.europa.eu.int/comm/employment_social/news/2005/jun/antidiscrimination_en.html)

## 02 JUNE

European Environment Agency: Children and Europe's continuing fight against air pollution: <http://org.eea.eu.int/news/Ann1117697382/index.html>

## 03 JUNE

External Relations: Monthly Calendar of the Barcelona Process - June 2005: [http://www.europa.eu.int/comm/external\\_relations/euomed/calendar.htm](http://www.europa.eu.int/comm/external_relations/euomed/calendar.htm)

## 06 JUNE

Employment and Social Affairs: Safety in new Member States' construction industry: [http://www.europa.eu.int/comm/employment\\_social/news/2005/jun/construction\\_en.html](http://www.europa.eu.int/comm/employment_social/news/2005/jun/construction_en.html)

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## 08 JUNE

The Commission initiates budgetary surveillance for Italy: [http://www.europa.eu.int/comm/economy\\_finance/about/activities/sqp/edp/edpit\\_en.htm](http://www.europa.eu.int/comm/economy_finance/about/activities/sqp/edp/edpit_en.htm)

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[http://www.europa.eu.int/comm/justice\\_home/doc\\_centre/immigration/work/doc\\_immigration\\_work\\_en.htm#com\\_2004\\_811](http://www.europa.eu.int/comm/justice_home/doc_centre/immigration/work/doc_immigration_work_en.htm#com_2004_811)

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[http://ue.eu.int/ueDocs/cms\\_Data/docs/pressData/en/ec/85349.pdf](http://ue.eu.int/ueDocs/cms_Data/docs/pressData/en/ec/85349.pdf)

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#### 24 JUNE

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#### 27 JUNE

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#### 29 JUNE

The European Commission recommends further steps under the excessive deficit procedure for Italy:  
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Employment and Social Affairs: 30 million EU citizens now carry the European Health Insurance Card:  
[http://www.europa.eu.int/comm/employment\\_social/news/2005/jun/card\\_en.html](http://www.europa.eu.int/comm/employment_social/news/2005/jun/card_en.html)

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## Expected events

After a hectic June, which was clearly dominated by the meeting of member state leaders at the European Council in Brussels, top EU bodies' discussions in July seem a bit dull. However, the two meetings of EU finance ministers in ECOFIN, which will indicate whether member states' uncompromising positions in the matter of the future common budget are or are not getting closer, will be very important.

<b>4.-7.6.2005</b>	<b>Strasbourg, France</b>
- European Parliament plenary session	
<b>6.-8.7.2005</b>	<b>Gleneagles, Scotland</b>
- EU Presidency - G8 Annual Summit	
<b>7.-8.7.2005</b>	<b>Belfast, UK</b>
Informal Council for Employment Ministers	
<b>11.-12.7.2005</b>	<b>Cardiff, UK</b>
- Competitiveness Informal	
<b>12.7.2005</b>	<b>Brussels, Belgium</b>
- Economic and Financial Affairs Council Meeting	
<b>15.7.2005</b>	<b>Brussels, Belgium</b>
- Economic and Financial Affairs Council (Budget) meeting	
<b>18.7.2005</b>	<b>Brussels, Belgium</b>
- General Affairs and External Relations Council	
<b>18.-19.7.2005</b>	<b>Brussels, Belgium</b>
- Agriculture and Fisheries Council	



In the last, June, issue of our EU News Monthly, we started the first part of an article that will be finished in the current issue and focuses on how the current challenges of European integration should be implemented into the Czech Republic's conditions. After detailed discussion of the possible fulfilment of the challenges in the area of efficiently functioning financial resources last time, we will now focus on the institutional environment having a favourable impact on healthy economic growth in the Czech Republic.

## EUROPEAN CHALLENGES FOR NATIONAL STRATEGY II

### INSTITUTIONAL BUSINESS ENVIRONMENT

A number of priorities should be targeted in the institutional environment area. The most sensitive priority for entrepreneurs themselves is **removing the complexity and non-transparency of the tax system** and decreasing the amount of the tax burden. The second priority concerns **strengthening competition in individual markets** and a feasible decrease of their over-regulation. The third, very important priority is **improving the quality of the public service provided**. The fourth priority is identifying **suitable market support tools** that will fulfil development priorities especially in the small and medium-sized business sector but also, more generally, in the entire business community. The fifth priority consists in a significant **improvement of the legislative environment quality**.

#### Priority No. 1 – Efficient tax system

Our tax system is characterized by **complexity, obscurity, non-transparency** and **instability**. In addition, the tax burden in direct taxes and health insurance and social security payments is rather high with respect to the growth potential of the Czech economy, even though a simple comparison of nominal tax rates in different countries does not lead to this conclusion.

#### Strengthening the transparency and simplicity of taxes

The ideal tax rule is **formulating unambiguous parameters** for each type of tax in a couple of paragraphs. They should expressly specify the tax rate, tax date and a couple of other key parameters. A tax exemption should correspond to the meaning of the word. It is therefore necessary to incorporate the fundamental mission of each tax in its basic parameters and any changes in the mission have to be implemented by re-adjusting the key parameters rather than adding another exemption.

Another difficult obstacle for taxpayers is the **constant amendment of tax rules** 'during the game' and completely **different interpretations** of the same issue by two or more tax offices. It is necessary to ensure that tax rules do not change over a longer period of time and that they are interpreted uniformly throughout the Czech Republic.

#### **Recommendations:**

- New tax regulations taking account of economic reality aspects in the context of the EU.

- Remove certain tax exemptions and deductible items especially in areas that are not the priorities of the individual pillars of this strategy.
- Simple and stable (permanent) interpretation of the tax rules by tax offices and other government authorities.
- Significantly increase and strengthen the informative functions of tax offices.

#### Cut direct tax rates

The environment of the European Union (Ireland, Estonia, Slovakia, etc.) as well as some of the current applicant countries (Romania) witnesses a **tax competition process** resulting in a considerable **cut of income tax rates** and **improvement of transparency** in tax rules. The Czech Republic must be a leader in the tax competition process. In particular the rate of the corporate and individual income tax has to visibly converge at the level of 20% (it is much lower in all of the above countries).

The importance of holding companies has been growing at the international level. Their occurrence is a measure of the quality of a business environment. The inflow of capital associated with the parent company's operations on a state's territory results in countries striving to create an **attractive environment for holding companies** on their territory. The tax law of the Czech Republic is only slightly acceptable for the parent companies of multinational holdings. The friendliness of tax parameters in this case means loosening the conditions for the exemption of dividend income arising from the relation between the parent company and its subsidiary, the exemption of capital income earned by selling a subsidiary and the extension of dividend and capital income exemption to cover subsidiaries from third countries.

#### **Recommendations:**

- Legislative change leading to gradually decreasing direct tax rates adequately to the tax competition process in the EU.
- Make holding company taxation more attractive.

#### Stabilizing the cut in the tax quota

Countries succeeding in the tax competition process focus mainly on the **direct taxes that are sensitive for investors**. For instance, the internationally applauded reform in Slovakia, while significantly cutting direct tax rates, resulted in a slight increase in the tax quota. The Czech Republic should be committed to **stabilizing the tax quota in the middle term**. However, in the very long term, after fulfilling structural reforms, it should not become resigned to the need to slightly decrease the total tax quota.



## Main topic

### Recommendations:

- Decrease the relative share of direct taxes in the overall tax collection.

### Internalizing externalities through taxes

There are a number of entities in the CR that deform the market environment without paying an appropriate price and exist at the expense of others; negative externalities are a reality among environmental polluters, with a number of entities negatively affecting the environment without paying for it. An example would be a municipality with gas installations where the minority of households insists upon heating by burning solid fuels, often completely unsuitable for heating. The same applies to exhaust fume pollution with vehicles that are not adequately environmentally-friendly or to undesirable waste treatment. It is absolutely essential to **tax such polluters effectively and prohibitively**. Similar procedures can be used e.g. for social system abuse.

### Recommendations:

- Tax instruments respecting ecological principles based on the quantification of negative externalities.
- Reducing social benefits to the subsistence level.

### Reducing secondary labour cost

International comparison indicates that a major competitive handicap in the Czech Republic is the **high level of secondary labour cost**. The share of income tax together with social security expenses averaged 43.6% of the overall labour costs in 2004 (as opposed to the OECD average of 36.5%). Labour taxation constitutes more than 50% of all tax revenues. The high progression of the individual income tax and the growing effective rate of taxation cause revenue redistribution in favour of people with a low level of savings here, which **restricts the creation of investment sources in the economy** in the upshot.

For employees as well as employers, this factor represents a visible barrier to the creation and extension of new job opportunities, flexible in terms of labour demand. It is therefore advisable to set about **lowering the social and health insurance contribution rates** while opening opportunities for alternative products and systems based on personal responsibility. In addition, it is advisable to quickly set about **setting a ceiling on the basis of assessment** for the two types of public insurance.

### Recommendations:

- Decrease the rates of social and health insurance contributions.
- Set a ceiling on the basis of assessment for social and health insurance.

## Priority No. 2 – Improving the competitive environment and eliminating obstacles

Market failures and insufficient competition in specific markets (network industries, transportation, agriculture, food industry) result in **higher prices or an insufficient quality** of products and services. The production of other products or services may negatively impact other parts of the economy (e.g. the production of electricity from fossil sources and their negative impacts on the environment, population health, labour market, etc.). The housing market and agriculture show over-regulation; this slows the development of a quality competitive environment and decreases the economic growth potential.

### Suppressing market failures

The competitive environment in the Czech economy shows 'distortions' in some markets, which bring about a loss of efficiency in the appropriate market mechanism. The main reason is an unbalanced structure of supply or demand in some industries, allowing local oligopolistic or monopolistic structures to occur. The loss of efficiency results in a decreased product or service quality and a higher price. The role of the public sector in the elimination of the failures can be summed up in these tools:

#### - **Weakening the monopolistic and oligopolistic structures in a targeted manner.**

This can be achieved by privatizing the remaining monopolies owned by the state. Where monopolies also control the infrastructure (CEZ, Czech Railways, etc.), the state must make regulatory provisions to ensure that other competitors have fair access to the infrastructure.

#### - **Creating and enforcing the basic rules of the game and conditions favourable for a competitive environment.**

In addition to effective legislation, it is also necessary to increase the efficiency of regulatory bodies (Energy Regulatory Office, Czech Telecommunications Office) so that their decisions do not strengthen the monopolistic or oligopolistic environment but ensure that there are 'fair' competition conditions in the markets.

#### - **Institutional effort to enlarge the markets both within and outside the EU.**

The largest possible market results in improved competition conditions and significantly lessens the strength of monopolistic and oligopolistic structures. Unlike with the above-mentioned public sector activities, most direct regulatory interventions in market mechanisms such as minimum or fixed purchase prices or minimum margins are



absolutely undesirable and do not lead to improvement; on the contrary, they aggravate the market failures.

#### Recommendations:

- Privatize the state's remaining majority interests in 'monopolistic companies' using the home capital market.
- 'Competitive environment development' – the main motto for all regulatory authorities' work, especially in network industries (Energy Regulatory Office, Czech Telecommunications Office).
- Increasing the frequency of inspections, introducing incentives for employees based on inspection efficiency (linking rewards to the quality of decisions).
- Eliminate the negative effects of public support for the competitive environment in a market.
- Support voluntary concentration (e.g. in the form of sales cooperatives, etc.) in markets with profound variations in the structure of supply and demand, allocating EU funds for these purposes.

#### Removing over-regulation

The public sector should create **conditions for the optimal functioning of market mechanisms** and only intervene in them in justified cases of emergency.

Price regulation in **rental housing**, not to mention its antisocial nature, affects economic relations through several channels. Above all, it is a barrier to workforce mobility, which negatively impacts the level of employment in a region and, on the other hand, results in a local lack of the necessary type of workforce. Furthermore, we cannot forget the negative externalities caused by regulation, with the cost of benefits for a group of economic entities (tenants) unjustly borne by other groups (home owners, young households and other entities seeking housing).

A markedly regulated sector in the Czech economy is agriculture. The Common Agricultural Policy is one of the basic pillars of the EU. Naturally, the Czech Republic is bound by it, so there is limited room for local measures. It is very important to **privatize land resources** as quickly as possible and increase the share of agricultural land owned by those who farm it.

In relation to the EU, it is necessary to give maximum support to the agricultural policy reform. The agricultural policy architecture needs to accentuate **environmental motives** and an **improvement of hygiene standards** as opposed to economic motives. On the other hand, farmers can get more legitimate support following the Polish example of health and social insurance payment exemptions or waivers, or their payment by the state.

#### Recommendations

- Deregulate rent.
- Make labour law more flexible, in particular by introducing broader contractual freedom in work contract conclusion and more opportunities for the unilateral termination of labour relations.
- Lessen the importance of direct subsidies to agriculture.
- Support the agricultural land market by guarantees for commercial loans or repurchase guarantees when using commercial loans to buy agricultural land.

#### Priority No. 3 – Providing effective and efficient public service

For entrepreneurs, the level of public service provided is one of the most important non-financial factors affecting business conditions. Economic growth is boosted by **improving the quality and efficiency of public service** while guarding the cost of its provision and simplifying communication processes between the state administration and private entities.

#### Improving the quality of public service provision and the efficiency of civil servants

Insufficient public service quality is seen as a major business obstacle especially by small and medium-sized business owners. Public administration officials do not realize that the users of their services are **their clients** and that they have to treat them as such. There is a lack of distinct relation between work quality and the reward earned.

The key to higher motivation is **adopting working rules from the private sector** where wages are determined by the employees' efficiency and competence. The end users (citizens, entrepreneurs) of the offices should have every opportunity to file complaints. Considerations of introducing job permanency may seem counter-productive. It should always hold true that selection will **only be based on professional qualities** and personal characteristics, not on political positions and party affiliation.





## Main topic

### Recommendations:

- Change the reward system in public administration in favour of a free agreement between the employee and the employer. Strengthen the link between wage and performance.
- Strengthen feedback between users and public service providers (opportunity to file effective claims, penalties, quality control).

### Achieving efficient public service performance by reasonable savings and the reduction of excessive capacities

On average, efficiency in public administration is lower than that in the private sector. Meeting the need for more efficient public administration operations will be possible thanks to **external audits** (organizational, functional, procedural and informational), performed by independent consulting companies. The common characteristic of institutions supported by the state budget is the inefficient use of budgeted funds. The largest volume of spending is always seen in December, when the institutions try to use up the allotted money. An attempt at preventing this was partially made by an amendment to the Budget Rules Act, which allowed transferring all unused money to reserve funds that may, however be used in subsequent periods.

### Recommendations:

- Have independent consulting companies perform organizational, functional, procedural and informational audits in all public administration bodies. Determine the optimal organizational and procedural structure of offices and the corresponding number of employees.
- Introduce a single procurement system for all public authorities at a centralized level, which has to be completed with strict anticorruption measures.

### Making citizens' and entrepreneurs' access to public service simpler and friendlier and getting rid of the administrative load

During registration as well as during regular business activities, entrepreneurs must communicate with and contact public authorities and institutions. They submit the same or very similar data to them time and again. Not only at the start but also during the course of their business activities, they have to bear an **enormous administrative load** from various points.

### Recommendations:

- Introduce Central Contact Points (CCPs) that would play the role of a single point of contact for entrepreneurs in their everyday communication with public administration.

- Unify or approximate the forms of different public authorities. Make the forms more widely available on the internet, where they can also be completed.

- A comprehensive solution to the problem should be provided by a global strategy for decreasing and measuring the administrative load on entrepreneurs, consisting in systematic measurement and analysis of the load that would be the basis of proposals for decreasing the load and keeping it at low levels.

### Expanding electronic communication with the public administration and supporting e-government

Electronic communication with the public administration is not yet sufficiently widespread. Its introduction on a wider basis would benefit both public authorities and private entities – it is **faster, cheaper** and **restricts room for corruption**. It is impeded by a low level of user knowledge of the possibilities of electronic signature, concerns over the security of shared information, relatively high purchase cost and insufficient offer of on-line governmental services. There is a lack of coordination in introducing information systems in public administration.

### Recommendations:

- Allowing all users to make any and all communication with public authorities over the internet and via e-mail. The state should use benefits to stimulate the use of e-communication with the state.
- Globally coordinating all of the public authorities' information systems used so far and newly purchased so that they can communicate and interconnect with one another without any problems.

## Priority No. 4 – Efficient use of market-conformable supporting public tools

The competitors' fight is becoming increasingly harsh, but another recent phenomenon is fierce competition among countries which are striving to stimulate the business activities of domestic and, in particular, foreign entities with various forms of public support beyond the scope of a quality institutional environment.

### Increasing the intensity of support for small and medium-sized businesses (SMBs); better utilization of the limited financial resources for their support and changing the focus of business support

While the conditions (especially in terms of finance) for foreign investors and large businesses have improved in recent years, there are still problems with SMBs' access to services and with the availability of capital for start-up enterprises. According to OECD studies, one of the major problems SMBs face is their isolation. The Czech

Republic lags behind in support for the association of companies and universities with a view to solving joint innovation and development projects. **Establishing a creative environment by supporting clusters** and supporting interfaces for cooperation between companies and universities is crucial for innovative business development.

While the intensity and amount of direct support for SMBs will always be subject to discussion, a more essential problem is the SMBs' access to high-quality and affordable consultancy and information services. The Czech Republic **lags behind in putting the best management practices into business practice**. A critical point for a wider expansion of SMBs is still their start-up phase; SMBs do not usually have funding problems when they have a credit history.

Employee education and qualification has to conform to the requirements related to technological development and innovations to ensure that the sector is competitive. The public support system should facilitate access to new forms of education for entrepreneurs and their employees.

#### Recommendations:

- Adopt a long-term, durable support programme for small and medium-sized business, independent of savings achieved in public budgets; make the volume of available funds provided under non-discriminating conditions as large as possible with respect to the efficiency of spending.
- Focus SMB support especially on those industries in which the regions and the entire Czech Republic are competitive. Pinpoint the clusters at regional and extra-regional levels and stimulate them further, directly and indirectly.
- Improve business access to affordable and highly qualified consulting services, thus supporting the introduction of best management practices and business development, and support employee qualification.
- Create an environment for start-ups that will facilitate founding new technology-oriented businesses, in particular by a wider involvement of venture capital.
- Harmony between labour market needs and the education system requires support for investments in education. There should be an individual element involved, in the form of tuition (including a system of guaranteed tuition loans). At the enterprise level, the tool should be a tax rebate (deduction) for investments in education.
- The volume of money provided by the state for science and research does not grow dynamically and the only solution may be to increase the volume and combine it with clearly specified efficiency criteria.

#### Improving the economy's export performance using pro-export policy tools

The Czech Republic is one of countries with a high share of import and export in the GDP; however, the SMBs' share in export is lower than usual in EU countries. The objective of a pro-export policy is **supporting business export** under conditions comparable to those in all developed countries. It is necessary to put more stress on indirect forms of support (Czechtrade) and consider an increase in volumes with direct support for export to 'exotic' countries, where the role of the state is irreplaceable. A process of the enlargement of trade and business agencies and improvement of the coordination and control of state economic services abroad is currently underway.

#### Recommendations:

- Both Export Guarantee and Insurance Corporation and Czech Export Bank face pressure from commercial competitors – it is necessary to improve the coordination and availability of linked pro-export services from a single point.
- Improve the coordination of promotion and presentation abroad, improve the efficiency of the promotion of the Czech Republic's interests abroad.

#### Priority No. 5 – Favourable legislative environment and improvement in law enforceability

Legislative environment and legal enforceability are one of the long-standing problems faced by the Czech Republic. At a general level, the **judicial system does not fulfil its main task sufficiently – providing citizens with quick justice**. The other side of the coin in judicial system problems is the legislative environment. Constant amendments to laws, permanent creation of new regulatory measures and their non-coordination also increase businesses' transaction cost.

From an entrepreneurial point of view, entry into business and forced exit from it are still dealt with insufficiently. Registration in the Commercial Register and insolvency proceedings take a long time in comparison with other European countries. A topic of its own is the fight against corruption. Corruption destroys the system of values in society, causes inefficiency in the economy and discriminates against certain groups of people in favour of others.

#### Improvement in law enforceability

There is no such thing as efficient and quick courts in the Czech Republic. Lawsuits take a long time and public trust





## Main topic

in the courts is low. This situation undermines one of the pillars of a functioning democratic society – the right to a quick and fair trial.

The problem of our judicial system is not a lack of judges but **bad court management**. A way out of the current situation is the internal reorganization of the judicial system that will transfer a part of the judges' work to specialized judicial personnel. Judges have to become more responsible for their performance.

### Recommendations:

- Reorganize the courts immediately in order to transfer a part of the judges' work to court officials and strengthen the judges' responsibility for their performance.

### Incorporating the impact analysis of new legislation in the law-making process

In developed countries, regulation is becoming one of important factors affecting the economy and its competitiveness. Although a certain rate of regulation is necessary and desirable, it is necessary to realize that any regulation brings about costs, both direct financial costs and requirements for human resources and time.

The Czech Republic's goal is not to create as many regulatory measures as possible; rather, the goal is their quality, ability to efficiently solve the problems at which they are targeted, and the acceptability of the price businesses have to pay to fulfil them.

To achieve this goal, newly created legislation should institutionalize **Regulatory Impact Assessment (RIA)** into the law-making process. RIA incorporation into the law-making process fully complies with OECD and EU recommendations and has been successfully implemented in many European countries.

### Recommendations:

- Introduce a transparent regulatory impact assessment process and publish the assessment.

### Adopting a new insolvency act

**Insolvency proceedings have been a long-term problem.** The situation has an impact on an overwhelming majority of businesses that will never be subject to insolvency proceedings but nevertheless bear the cost of a higher risk for creditors in the price of debt financing.

Insolvency proceedings must be designed to have the **creditors decide** on the method of handling bankruptcy and decisions of commercial nature have to be put, in situations where both solutions are possible, into the hands of the market.

### Recommendations:

- Adopt a bankruptcy act that will strengthen the position of creditors and provide for more extensive market functioning during the bankruptcy process.

### Commercial Register and entry into business

Entry into business is complicated by multiple registration for both individuals and legal entities. Therefore, the registration processes have to be **consolidated with a single authority and preferably using a single form**.

The speed of company establishment is currently below average in comparison with other OECD countries. According to the World Bank, establishing a company in the Czech Republic requires 40 days and 10 procedures, while in most developed countries it is a matter of several days and half the number of procedures.

At the moment, the system of incorporation in the Commercial Register is fully in the hands of a court that has to review all the documents needed for incorporation.

Following the example of other countries, the system needs to be changed completely, by abandoning factual review and **introducing a registration principle** while specifying deadlines for incorporation in the Commercial Register.

### Recommendations:

- Introduce a registration principle as opposed to the factual review principle into incorporation in the Commercial Register and speed up the incorporation process.

- Simplify the process of entry into business for individuals; consolidate the administrative agenda of tax offices, trade licensing offices and social security offices.

### Eliminating corruption

Corruption is seen as a big problem in the Czech Republic. The fight against corruption has to become one of the Government's priorities and must be put up conceptually and forcefully. The state has to be committed to **eliminating risky processes**, both by changes in the processes and legal regulations, and place the most emphasis on officials' responsibility for their work.

### Recommendations:

- Adopt new conflict of interest legislation.

- Systematically eliminate opportunities for corruption and risky processes in public administration, e.g. by introducing e-government elements, eliminating over-regulation and setting obligatory limits.



During the first half of 2005, the British economy may boast of characteristics that put it markedly above the European average both from the momentary or short-time point of view and in long-term monitoring. The above-average level then can be applied not only to variables that can be quantified but also to processes that are usually valued rather subjectively, using the indicators of trust and quality in the business and investment environment.

## UNITED KINGDOM

### Key indicators

<i>Government type/chief of state</i>	constitutional monarchy/The queen Elisabeth II.
<i>Area (share of EU)</i>	224 820 km2 (5.65%)
<i>Population (share of EU)</i>	59 673 100 (13.06 %)
<i>Age structure</i>	0-14 years: 18.3%, 15-65 years: 65.8%, over 65 years: 15.9%
<i>Total GDP (share of EU)</i>	EUR 1 709.75 bn (16.65 %)
<i>GDP per capita in PPS</i>	118.4 % of EU-25 average
<i>GDP - composition by sector</i>	agriculture: 1.0%, industry and construction: 25.4%, services: 73.6%
<i>Average inflation</i>	1.3%
<i>Average unemployment</i>	4.6%
<i>GDP growth</i>	3.1%
<i>General government balance</i>	-3.2% of GDP
<i>General government debt</i>	41.6% of GDP
<i>Number of NUTS2, the richest and poorest NUTS2 (in terms of GDP per capita in PPS to EU)</i>	37 NUTS2, Inner London (315.4%), Hampshire and Isle of Wight (72.6%)

Note: the figures are for 2004, source: EU, CIA

### Commentary

Although the UK is an economy that is markedly **rich** in comparison with the EU-25, with a GDP per resident amounting to 118.4% of the EU average in 2004, it is also a **dynamically developing** and growing economy.

For more than two centuries the United Kingdom has been one of the world's leading economies. The **manufacturing industry** was typical for the British economy for many years, in spite of the fact that the country does not have enough raw material resources. The United Kingdom has also been characterized by a relatively small extent of otherwise highly intensive and productive agriculture. Thus British economic development has been based mainly on exports of manufacturing industry products, and in the last ten years services, and on the import of raw materials and food. The manufacturing industry has undergone very significant structural changes and **modernization** during the last twenty years or so. Now it can rely on well-developed mechanical engineering, power plant facilities, transport technology, restructured shipbuilding industry, electrical engineering and communication devices and the chemical industry.

The UK's economic power is concentrated mainly in **strong urban agglomerations** in which more than a third of its population lives. The strongest and richest of them – London – is also the richest region in the entire EU.

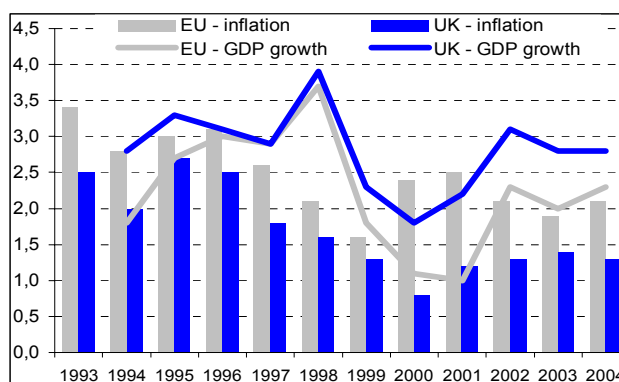


A special UK feature in comparison with the continental European countries is the structure and territorial **orientation of the openness of the British economy**. Until the early '70s, the UK's most important business partner was the United States. Since the mid-70s, the orientation of the British foreign trade has been focusing more on European Community countries; even now, however, after the last EU enlargement in May 2004, the EU share in the British foreign trade amounts to slightly more than 50%. The most important business partner at the moment is Germany, followed by France and the Netherlands.

The British economy achieved an annual growth of 3.0% in the fourth quarter of 2004 and had grown at a 3% or higher rate in the previous three quarters as well. Another positive feature of the British economic development is a **low rate of inflation**. During the last year, British inflation was always lower than 2.0%. The British economy then may boast another favourable asset: it is also an economy with a **lower rate of unemployment** than the EU average. The UK is also one of those EU economies that have a relatively low public debt in comparison with the GDP, but whose budget deficit only barely remains below the limit of 3% of the GDP.

At a glance, the UK's role in the system of EU **does not match the role of comparable countries** such as Germany or France. On the other hand, the UK's specific position is characterized by a very successful pragmatic approach, manifesting itself e.g. in British entities' very high yield when drawing on EU funds. A number of specific arrangements and very important EU documents have also resulted from the UK's specific demand. Particularly known is the **reserved approach to monetary and social integration**.

### Inflation and GDP



Source: Eurostat



# Statistical window

The statistical window in a tabular form shows the important macroeconomic and financial indicators of the countries which have newly acceded to the European Union, with respect to the criteria defined in the Maastricht Treaty: the month-on-month, year-on-year and average inflation rates, the indicators of the fiscal budget deficit and the state debt, expressed in relation to the GDP, and the volatility of the exchange rates of national currencies to the euro.

## Price development

	m-on-m HICP growth			y-on-y HICP growth			average y-on-y HICP growth in %		
	III-05	IV-05	V-05	III-05	IV-05	V-05	III-05	IV-05	V-05
<b>EU</b>	0.6	0.4	0.2	2.1	2.1	1.9	2.2	2.2	2.2
<b>EU - minimum</b>	-	-	-	-	-	-	0.7	0.8	0.8
<b>CR</b>	-0.1	0.3	0.1	1.2	1.4	0.9	2.4	2.3	2.2
<b>Estonia</b>	0.6	0.5	0.2	4.8	4.7	2.9	4.0	4.3	4.2
<b>Cyprus</b>	0.9	1.1	0.2	2.4	2.8	2.0	2.3	2.5	2.6
<b>Lithuania</b>	0.6	0.3	0.2	3.3	3.2	1.9	2.2	2.5	2.6
<b>Latvia</b>	0.6	1.1	0.8	6.6	7.1	6.5	6.8	7.0	7.0
<b>Hungary</b>	0.5	0.7	0.6	3.3	3.8	3.5	6.0	5.7	5.3
<b>Malta</b>	0.5	3.6	0.6	2.6	2.0	2.4	2.7	2.6	2.5
<b>Poland</b>	0.1	0.4	0.3	3.4	3.1	2.2	4.0	4.1	4.0
<b>Slovenia</b>	-0.1	0.2	0.1	2.3	2.5	2.3	6.0	5.6	5.1
<b>Slovakia</b>	1.0	0.1	0.3	3.3	2.7	2.1	3.4	3.4	3.2

Note: HICP means harmonised index of consumer prices, EU – minimum means the average inflation in three EU member states with the lowest inflation. Source: Eurostat

## Fiscal development

	Net balance of general government to GDP in %			General government gross debt to GDP in %		
	2002	2003	2004	2002	2003	2004
<b>EU-25</b>	-2.2	-2.8	-2.6	62.7	64.3	63.8
<b>CR</b>	-6.8	-11.7	-3.0	30.7	38.3	37.4
<b>Estonia</b>	1.4	3.1	1.8	5.3	5.3	4.9
<b>Cyprus</b>	-4.5	-6.3	-4.2	65.2	69.8	71.9
<b>Lithuania</b>	-1.5	-1.9	-2.5	22.4	21.4	19.7
<b>Latvia</b>	-2.7	-1.5	-0.8	14.1	14.4	14.4
<b>Hungary</b>	-8.5	-6.2	-4.5	55.5	56.9	57.6
<b>Malta</b>	-5.9	-10.5	-5.2	62.7	71.8	75
<b>Poland</b>	-3.6	-4.5	-4.8	41.2	45.4	43.6
<b>Slovakia</b>	-5.7	-3.7	-3.3	43.3	42.6	43.6
<b>Slovenia</b>	-2.4	-2.0	-1.9	29.5	29.4	29.4

Note: according to the ESA 95 methodology. Source: Eurostat

## Volatility of FX rates of new EU member states

	average rate	Last 24 months		average rate	Last 12 months	
		deviation maximum in %	deviation minimum in %		deviation maximum in %	deviation minimum in %
<b>Czech koruna</b>	31.51	+7.4	-5.4	30.73	+4.8	-3.6
<b>Estonia kroon</b>	15.65	+0.0	+0.0	15.65	+0.0	+0.0
<b>Cyprus pound</b>	0.582	+1.5	-0.9	0.579	+1.0	-0.9
<b>Lithuanian litas</b>	3.453	+0.0	-0.0	3.453	+0.0	-0.0
<b>Latvian lats</b>	0.668	+6.9	-4.3	0.683	+4.6	-2.2
<b>Hungarian forint</b>	252.7	+4.6	-7.8	247.4	+2.4	-3.0
<b>Maltese lira</b>	0.429	+1.1	-1.4	0.430	+1.2	-1.1
<b>Polish zloty</b>	4.416	+13.9	-10.5	4.209	+8.6	-7.1
<b>Slovakian koruna</b>	40.04	+6.6	-5.5	39.19	+4.4	-2.6
<b>Slovenian tolar</b>	238.3	+1.9	-0.7	239.8	+0.1	-0.1

Note: volatility of foreign exchange rates of new EU member states to euro is expressed in the form of arithmetical average and in the form of maximum and minimum deviation from the average in the reference periods. The reference periods end at 30 June 2005. Source: Eurostat

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