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SPICe Briefing

The European Union – The Budget

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This subject profile provides details of the way in which the European Union budget is agreed and then how it is collected.

Image: European Parliament

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THE EUROPEAN UNION BUDGET

As with all international organisations the European Union requires a budget. The budget pays for the EU's running costs and more importantly finances the EU's strategic policy programmes such as structural funds and research and development funding.

HOW THE BUDGET IS AGREED

In the first instance, the European Commission puts forward a proposal for an overall EU budget covering a number of years, this is known as the multiannual financial framework. The multiannual financial framework is designed to ensure that "Union expenditure develops in an orderly manner and within the limits of its own resources" (Article 312 of the Treaty on the Functioning of the European Union). Crucially, the European Union can only spend the money it raises and cannot go into deficit. The multiannual financial framework is required to last for at least five years. Recent frameworks have lasted for seven years including the current one which will run until the end of 2013.

The multiannual financial framework must be agreed unanimously by the Council of Ministers and must receive the consent of the European Parliament. According to Article 312(3) of the Treaty on the Functioning of the European Union; "the financial framework shall determine the amounts of the annual ceilings on commitment appropriations by category of expenditure and of the annual ceiling on payment appropriations. The categories of expenditure, limited in number, shall correspond to the Union's major sectors of activity."

Within these categories, it is for the Council of Ministers and the European Parliament to agree on the specifics of the budget for each year. Article 314 of the Treaty on the Functioning of the European Union outlines the process for agreeing the Annual Budget. It broadly follows the same approach as the Ordinary Legislative Procedure.

The European Commission is required to submit a proposed draft budget to the European Parliament and the Council by 1 September of the year preceding the year for which the budget will apply. Following this, the Council has one month (until 1 October) to agree its position on the budget and forward this, along with the reasons for its position to the European Parliament. The European Parliament then has forty two days to either agree the Council position or to adopt amendments (by a majority of its members).

At this point, the difference between the Ordinary Legislative Procedure and the procedure used to agree the annual budget is activated. Instead of going to a second reading in the Council and the European Parliament, a Conciliation Committee is established by the European Commission to find an agreement between the Council and the European Parliament. The Conciliation Committee has fourteen days to agree a common position.

If a common position is agreed, the Council and the European Parliament has fourteen days to agree the text or to reject it. The European Parliament must approve the text for it to be adopted. If the Council chooses not to approve the text, it can still be adopted if the European Parliament "acting by a majority of its component members and three-fifths of the votes cast, decide to confirm all or some of the amendments…..Where a European Parliament amendment is not confirmed, the position agreed in the Conciliation Committee on the budget heading which is the subject of the amendment shall be retained." (Article 314(7(d)) Treaty on the Functioning of the European Union) In this instance the budget would be deemed to be adopted despite not having the backing of the Council.

FINANCING THE BUDGET

Article 311 of the Treaty on the Functioning of the European Union states that; “The Union shall provide itself with the means necessary to attain its objectives and carry through its policies”. Article 311 goes on to state that “without prejudice to other revenue, the budget shall be financed wholly from own resources”.

Previously the European Union’s budget had depended entirely on contributions from member states own national budgets. Introducing a system of own resources meant the European Union became financially independent. This is because own resources are sources of finance which accrue automatically to the European Community from member states.

The budget is financed by member states in three different ways. Through “Traditional Own Resources” which is customs revenue generated for the European Union by Community legislation, through Value Added Tax resources and through a system linked to GNI.

The GNI-based contribution is the largest part of each member state’s payment and is set each year by the EU to balance the budget.

Traditional Own Resources

Traditional Own Resources (TOR) are sources of revenue generated exclusively by the European Commission as a result of European Community legislation. For example, European Community customs legislation which governs customs duties on goods (including agricultural produce) imported into the European Union provide for a common customs tariff which is collected by member states who receive a percentage of the resources as compensation for collecting them.

Value added tax

In 1970, Value Added Tax (VAT) resources were introduced to supplement the budget which had previously relied only on traditional own resources. However, due to delays trying to agree a VAT base figure the VAT resource did not come into use until 1980.

The resource based on (VAT) is a uniform percentage rate that is applied to each member state’s harmonised VAT revenue. The VAT resource is currently calculated at 0.33% of each member state’s tax base. The tax base is a theoretical construct that compensates for the fact that neither the VAT rate nor the list of goods and services covered by VAT are harmonised at EU level.

Gross national income

The GNI own resource (originally Gross National Product) was introduced in 1988. One of the main reasons for its introduction was to introduce a new resource to balance the budget and ensure the European Union was able to raise as much money as it needed to spend. This is important because the EU budget must always be in balance. The GNI resource is a uniform percentage rate (currently 0.73%) applied to the GNI of each member state.

Correction Mechanisms

Correction mechanisms have been introduced into the budgetary system of the European Union. They are designed to correct excessive contributions by certain Member States. Perhaps the most famous correction mechanism is the United Kingdom rebate. The United Kingdom has received a rebate from the EU budget since 1984. At that time the then Prime

Minister Margaret Thatcher successfully negotiated the rebate because the United Kingdom was the third poorest member of the EU but was on course to become the biggest net contributor to the budget.

The abatement means the UK is reimbursed by 66 % of the difference between its contribution and what it receives back from the budget. The cost of the UK rebate is divided among EU Member States in proportion to the share they contribute to the EU's GNI though a number of the other net contributors to the EU budget (Germany, the Netherlands, Austria and Sweden) pay proportionally less than their share.

The UK rebate has had wider implications and in recent years had led to other member states receiving various “correction mechanisms” to ensure that they did not pay more than their share into the budget. In order to reach agreement of each Multi-annual Financial Framework agreement is also now required on a number of correction mechanisms. This has made the budget process very confusing. Another criticism of the current system is that the correction mechanisms involve money being returned to the more prosperous member states largely at the expense of the less prosperous ones.

During the 2014-2020 Financial Framework the following corrections apply:

- Denmark, the Netherlands and Sweden will benefit from gross reductions in their annual GNI contribution
- Austria will benefit from gross reductions in its annual GNI contribution in 2014, 2015 and 2016.
- Germany, the Netherlands and Sweden will benefit from a reduced VAT call rate of 0.15%

Figures from the European Commission (2013a) and reproduced in Table 1 shows the breakdown by the different sources of revenue for the 2013 and 2014 EU budgets.

	2013		2014	
Type of revenue	EUR million	%	EUR million	%
Customs duties and sugar levies	14 822.7	10.3	16 310.7	12.0
VAT-based resource	14 680.1	10.2	17 882.2	13.2
GNI-based resource	110 822.8	76.7	99 767.3	73.6
Other revenue	4 125.2	2.9	1 544.4	1.1
TOTAL	**144 450.8**	**100.0**	**135 504.6**	**100.0**

THE 2014-2020 BUDGET

On 2 December 2013, the Council of the European Union adopted the regulation laying down the EU's multiannual financial framework (MFF) for 2014-2020.

The Multiannual Financial Framework (MFF) lays down the maximum annual amounts ('ceilings') which the EU may spend in different political fields ('headings') over a period of no less than five years. The current MFF covers seven years: from 2014 to 2020 and sets a budget ceiling of €960 billion.

The MFF is not the budget of the EU for seven years. Rather, it provides a framework for financial programming and budgetary discipline, ensuring that EU spending is predictable. It also allows the EU to implement common policies over a period that is long enough to make them effective. By defining how much and in which areas the EU should invest over seven years, the MFF is an expression of political priorities as much as a budgetary planning tool. The annual budget is adopted within this framework and usually remains below the MFF expenditure ceilings in order to retain some margin to cope with unforeseen needs.

THE MULTIANNUAL FINANCIAL FRAMEWORK PRIORITIES

The MFF is divided into six categories of expenditure ('headings') corresponding to different areas of EU activities (European Commission 2013b):

<u>1. Smart and Inclusive Growth</u>

1a. Competitiveness for growth and jobs: includes research and innovation; education and training; trans-European networks in energy, transport and telecommunications; social policy; development of enterprises etc.

1b. Economic, social and territorial cohesion: covers regional policy which aims at helping the least developed EU countries and regions to catch up, strengthening all regions' competitiveness and developing inter-regional cooperation.

<u>2. Sustainable Growth</u>

Natural Resources: includes the common agricultural policy, common fisheries policy, rural development and environmental measures.

<u>3. Security and citizenship</u>

Includes justice and home affairs, border protection, immigration and asylum policy, public health, consumer protection, culture, youth, information and dialogue with citizens.

<u>4. Global Europe</u>

Covers all external action ("foreign affairs") by the EU such as development assistance or humanitarian aid. The European Development Fund also provides financial resources for the ‘EU as a global actor’. However, it is not part of the EU budget and therefore does not fall under the MFF.

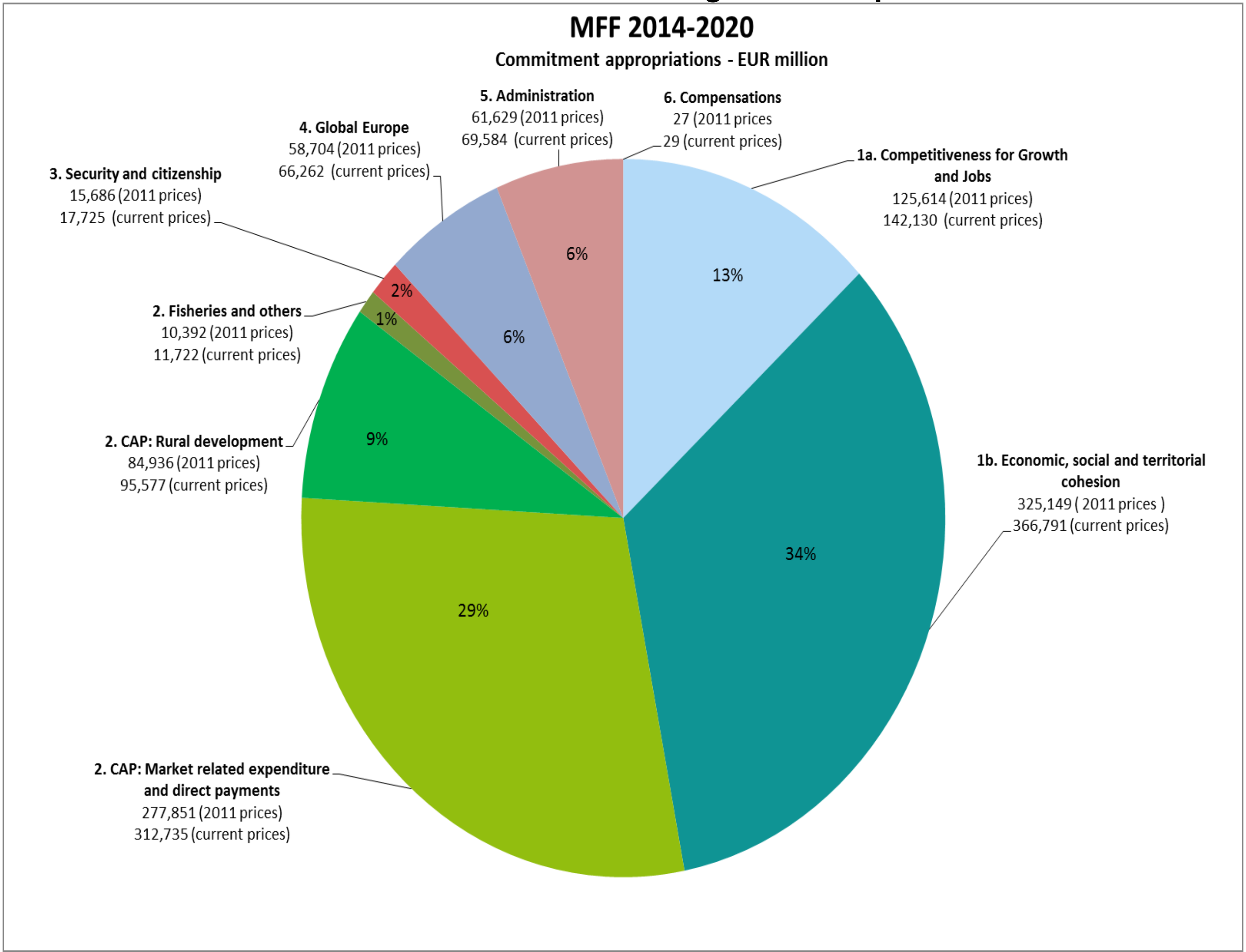
<u>5. Administration</u>

Covers the administrative expenditure of all the European institutions, pensions and European Schools.

6. Compensations

A temporary cash flow mechanism designed to ensure that Croatia, who joined the EU in July 2013, does not contribute more to the EU budget than it benefits from it in the first year following its accession.

Multiannual Financial Framework 2014-2020: Categories of Expenditure



(European Commission 2013a)

United Kingdom Contributions to and Receipts from the EU Budget

HM Treasury (2015) has produced figures showing how much the UK has paid towards the EU Budget and how much it has received back. The figures are for 2009 to 2015 and are reproduced in the table below. The figures confirm that the UK is consistently a net contributor to the European Union.

The UK's net contribution to the EU Budget (£million)

	2009 Outturn	2010 Outturn	2011 Outturn	2012 Outturn	2013 Outturn	2014 Outturn	2015 estimated outturn*
Gross Payments**	14,129	15,197	15,357	15,746	18,135	18,777	17,779
Less UK Rebate	-5,392	-3,047	-3,143	-3,110	-3,674	-4,416	-4,861
Less Public Sector Receipts	-4,401	-4,768	-4,132	-4,169	-3,996	-4,576	-4,445
Net Contributions to the EU Budget	4,336	7,382	8,082	8,467	10,465	9,785	8,473

*The figures for 2015 are based on the Office for Budget Responsibility Forecast Supplementary Table (2.24) and converted to sterling. It has been adjusted to take into account the late adoption of amending budget 8 to the 2015 annual budget. Those for earlier years are outturns.
**Gross payment figures include TOR payments at 75 per cent. The remaining 25 per cent is retained by the UK to cover the costs of administering collection on behalf of the EU.

According to HM Treasury, the volatility of the UK's net contribution to the EU Budget from year to year results from "variations in payments made due to the nature of the Own Resources system; variations in public sector receipts; consequent fluctuations in the UK's rebate; and the exchange rate".

Another aspect to remember about the UK's recorded receipts from the EU budget are that the Treasury notes only those public sector receipts. The UK is also a recipient of funding which goes directly to the UK private sector, such as funding for research paid directly to UK universities. The Treasury numbers capture only those receipts that pass through the UK public sector.

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