Recent developments in Germany's financial relations with the European Union

Transfers of funds from the Federal Republic to the EU budget increased sharply up to the mid-nineties; since then they have largely stabilised. At almost DM 24 billion in 1998, the net payment to the European Union recorded in the balance of payments statistics was slightly higher than in 1992[1], but as a percentage of the gross national product it had decreased. In addition to the accession of new "net contributors" in 1995, this development was mainly due to the fact that the German gross national product increased less sharply than in the Community as a whole. Furthermore, the resulting subdued increase in transfers to the EU contrasted with rapidly rising backflows from the Community budget's Structural Funds especially benefiting the new Länder. However, the level of the German net payment is still high compared with the other member states. Following the financial decisions taken by the European Council at the end of March, some relief is expected for Germany by the year 2006.

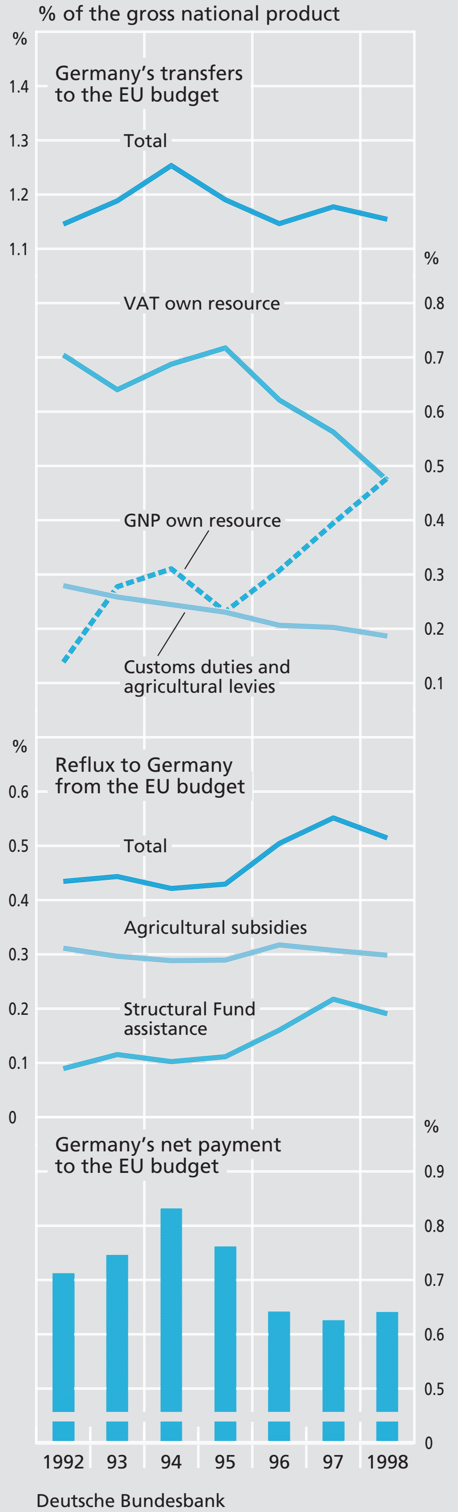
Transfers to the EU budget between 1993 and 1998

Reduction of the German financing share ...

As a supranational budget-making body, the European Union continued to require consid-

1 This article is a follow-on to an earlier report which covered the period up to 1992. See: Deutsche Bundesbank, The financial relations of the Federal Republic of Germany with the European Communities since 1988, Monthly Report, November 1993, page 61 ff.

Financial relations between Germany and the EU



erable additional funds from its member states to finance its growing budget between 1993 and 1998. During this period, the total volume of Community spending rose by an annual average of 5½ % to almost ECU 81 billion. By contrast, the German contribution to the Community budget only increased by an annual average of just over 3 % (varying substantially in some years) during this period. This contribution corresponded to a largely constant share of just over 1.1% of the German gross national product.[2] Also in terms of the total revenue of all German central, regional and local authorities, the financing share has stabilised (at roughly 3¾ %) since 1993. Hence, the German financing share in the Community budget has decreased over the last four years. Germany accounted for as much as one-quarter of the Community's total own resources in 1998, whereas its highest share had been one-third in 1994.

... and its causes

There were two major reasons for this development. Following the accession of Austria, Sweden and Finland in 1995, a larger number of member states now contribute to financing the EU budget. In addition, Germany's relative prosperity within the EU has deteriorated over the last few years. Up to 1995 the growth of Germany's nominal gross national product, expressed in ECU – the unit of account used for calculating the financing shares – was higher than average owing to the appreciation of the Deutsche Mark vis-à-vis other European partner currencies. How-

2 Since the determination of the member states' contribution is mainly based on the gross national product (GNP), the GNP (rather than the more frequently used gross domestic product) will be used as a measure in this article.

Financial transactions between the EU and Germany

DM billion

Item	1992	1993	1994	1995	1996	1997	1998
Payments to the EU general budget							
Customs duties and agricultural levies	8.8	8.4	8.3	8.1	7.4	7.5	7.1
VAT own resource	22.0	20.5	23.0	24.8	21.9	20.4	17.8
GNP own resource	4.5	9.0	10.5	8.1	10.9	14.4	18.0
Other 1	0.4	0.0	0.0	0.0	0.0	0.3	0.2
Total	35.7	37.9	41.8	41.0	40.3	42.6	43.2
Change from previous year in %	8.0	6.1	10.5	– 2.0	– 1.7	5.7	1.4
Memo item							
Germany's financing share in % 2	30.2	29.8	33.3	31.4	29.2	28.2	25.1
Payments out of the EU general budget							
Relating to agricultural policy	9.8	9.6	9.8	10.1	11.3	11.3	11.3
Relating to structural policy 3	2.9	3.8	3.6	4.0	5.8	8.0	7.3
Refund of collection costs	0.9	0.8	0.8	0.8	0.7	0.7	0.7
Total	13.6	14.2	14.2	14.9	17.8	20.1	19.3
Change from previous year in %	– 2.6	4.4	– 0.3	5.1	19.7	12.4	– 3.6
Memo item							
Germany's reflux share in % 4	14.0	12.7	14.8	13.6	14.8	14.1	...
Net payment to the EU budget	22.0	23.6	27.6	26.1	22.4	22.5	23.8

Source: Deutsche Bundesbank, balance of payments statistics; European Commission; European Court of Auditors, annual reports for various financial years; Bundesbank calculations. — **1** Including co-responsibility levy and super levy for milk, milk products and cereals. — **2** German share in the own resources which are actually available. — **3** Specifically, the European Regional Development Fund (ERDF), European Social Fund (ESF), European Agricultural Guidance and Guarantee Fund, Guidance Section (EAGGF Guidance). — **4** German share in the operational payments from the EU budget to the EU member states, excluding unassignable payments.

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ever, it subsequently increased at a much slower pace than in the Community as a whole because of weaker nominal economic growth and the declining external value of the Deutsche Mark.

Breakdown of transfers

In the last few years, considerable shifts have occurred in Germany's transfers to the EU budget. While the GNP-based "residual source of financing", which dates back to the late eighties, initially only accounted for one-eighth of the total German contribution to the EU budget (at DM 4½ billion in 1992), this share rose to just over two-fifths (DM 18 billion) last year. The reason for this increase was the Own Resources Decision, which took effect at the beginning of 1995 and implemented the financing regulations adopted at the Edinburgh summit in December 1992.

GNP own resource

These Council decisions included an expansion of the financial framework to be achieved by progressively raising the ceiling for the total own resources from 1.20 % to 1.27 % of GNP by the year 1999. In addition, they aimed at a modification of burden-sharing in favour of the less well-off member states. This objective was to be achieved by reducing the share of the own resource based on the value-added tax, which was considered outdated, and by raising the financing share of the GNP own resource, which was more in line with the ability-to-pay principle.[3] This change in the financing system was implemented step by step and had a growing

3 For this purpose, the maximum "call-in rate" of the value-added tax was reduced from 1.4 % to 1.0 % of the harmonised base, and the capping limit of the VAT base was lowered from 55 % to 50 % of GNP.

impact on the German transfers to the Community budget.

VAT own resource

As a consequence of these new financing regulations, the growing contribution to the GNP-based "residual source of financing" coincided with a decrease in the importance of the VAT own resource. Last year the latter only accounted for just under DM 18 billion or 41% of the total German financing share, whereas it had still amounted to DM 22 billion, i.e. more than three-fifths of the total transfers to the EU budget, in 1992. Since Germany's share in the Community's VAT base was slightly higher than in the EU's national product, the changed financing structure of the EU budget, on balance, has brought moderate relief for the Federal Republic over the last few years.

Customs duties and agricultural levies

During the nineties, the significance of the traditional own resources – customs duties and agricultural levies – gradually diminished. German proceeds from these items only amounted to just over DM 7 billion in 1998, which corresponds to one-sixth of the total German financing share. At almost DM 9 billion, this revenue had still accounted for approximately one-quarter of the German transfers in 1992. This decline mainly reflects the further liberalisation of world trade and the concomitant lower customs duties, including those at the Community's external borders.

Transfers from the EU budget

More back-flows ...

Whereas the increase in German payments to the Community budget has slowed down over the last few years, the back-flows from the EU budget to German beneficiaries have risen sharply, particularly since 1995. On balance – although starting from a relatively low level – they increased by an annual average of 6% between 1993 and 1998, i.e. almost twice as much as the German payments to the Community budget.

... from the Structural Funds especially for eastern Germany

This development is attributable to the growing inclusion of eastern Germany in the assistance schemes of the Structural Funds, the resources of which had been increased considerably for the period between 1994 and 1999 at the European Council meeting in Edinburgh. Under transitional provisions the new Länder initially received ECU 3 billion worth of Structural Fund assistance up to 1993 through a special programme. From 1994 onwards, they were fully integrated in the general promotion schemes of the relevant funds (Regional Fund, Social Fund, Guidance Section of the Agricultural Fund). The east German Länder (including East Berlin) especially benefited from being generally classified as "Objective 1 regions". This primary assistance is designed for less advanced regions with a per-capita GDP which is more than 25% lower than the EU average. At roughly ECU 94 billion (at 1994 prices), this assistance category alone accounted for around three-fifths of the Structural Fund resources between 1994 and 1999. In this context, as much as just over ECU 13.6 billion of the EU's financial plan for this period were allocated to eastern Germany. Half of these payments are made by the Regional Fund; they are used as co-financing funds together with the shares of the Federal and the Länder

Expenditure and receipts of the EU general budget

Item	1992	1993	1994	1995	1996	1997	1998 pe	1999 1	1992	1999
	ECU billion							€ billion	Percentage of total	
Expenditure										
Agricultural policy	31.2	34.4	33.6	34.5	39.1	40.6	38.8	40.9	53.3	47.9
Structural policy	18.9	20.9	16.5	20.1	25.3	27.0	29.2	31.4	32.3	36.7
Internal policies	2.5	2.8	3.2	3.2	3.7	4.0	4.0	4.1	4.2	4.8
External actions	2.2	2.8	3.2	3.4	3.8	4.0	4.1	4.3	3.7	5.0
Reserves	0.9	0.0	0.3	1.8	0.9	0.5	0.4	0.3	1.5	0.4
Administrative expenditure	2.8	3.3	3.6	3.9	4.0	4.1	4.2	4.5	4.9	5.3
Total	58.6	64.2	60.3	66.9	76.8	80.2	80.6	85.6	100	100
Change from previous year in %	8.9	9.6	– 6.1	11.0	14.7	4.5	0.5	5.8	.	.
Receipts										
Agricultural levies 2	2.0	1.9	2.1	1.9	1.8	1.9	2.0	1.9	3.3	2.2
Customs duties 2	11.3	11.1	11.2	12.5	11.8	12.2	12.2	11.9	18.9	13.9
VAT own resource	34.7	34.5	33.3	39.2	36.4	34.2	33.1	30.4	58.0	35.5
GNP own resource	8.3	16.5	17.7	14.2	21.1	26.9	35.0	39.3	13.9	45.9
Other receipts 3	3.5	1.7	1.8	7.2	10.2	5.3	2.3	2.1	5.8	2.5
Total	59.7	65.7	66.0	75.1	81.3	80.5	84.5	85.6	100	100
Change from previous year in %	6.2	10.0	0.5	13.7	8.3	– 0.9	4.9	1.2	.	.
Budgetary balance	1.1	1.5	5.7	8.2	4.5	0.3	3.9	–	.	.

Source: annual reports of the European Court of Auditors, European Commission and Bundesbank calculations. — **1** Budget (funds for payments). — **2** Net, i.e. less the collection costs refunded to the member states. — **3** Including available surpluses from the previous financial year.

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Governments for the Joint Task "Improving the Regional Economic Structure" to promote public-sector investment in business and industry. In addition, agricultural reform in the new Länder is also being promoted through assistance by the Social Fund and the Guidance Section of the Agricultural Fund. Furthermore, the Social Fund promotes vocational training schemes. In total, around two-thirds of the Structural Fund assistance granted to Germany, i.e. ECU 22 billion, are channelled to the new Länder, although a substantial share of this amount had not yet been paid out by end-1998. Of late, Structural Fund assistance allocated to Germany was two and a half times as high as in 1992.

Declining weight of agricultural subsidies in the EU budget

Largely in line with the spending priorities adopted by the European Council, the increase in the EU's expenditure on agricultural policy was lower than average. Nonetheless, at ECU 39 billion, spending in the context of the agricultural market regulations (Guarantee Section of the Agricultural Fund) still accounted for 48 % of the Community's 1998 budget, compared with just over 53 % in 1992 and more than 60 % during the eighties. Between 1993 and 1998 agricultural market expenditure basically remained within the specifications of the agricultural guideline, i.e. below a spending ceiling which is adjusted annually by 74 % of the expected growth rate of the Community's gross national product. It was even possible to finance the additional spending temporarily required for the realignments in the European Monetary System out of this source. The monetary reserve which had been provided as a precaution was never drawn on. The curbing of expenditure growth in the agricultural sector also reflects agricultural policy reform measures introduced in 1992. For instance, the intervention prices for important agricultural products were temporarily lowered, while farmers were granted more direct aid than before.

Agricultural back-flows to Germany

The decreasing share of agricultural market expenditure in the Community budget was also evidenced by the development of agricultural assistance to Germany. Even though it still accounted for the biggest share of the back-flows, the total amount was only stepped up moderately, i. e. from almost DM 10 billion in 1992 to just over DM 11 billion last year. As a result of a more market-oriented agricultural pricing policy and owing to changed world market conditions, the expenditure on refunds for exports to third countries dropped drastically. In Germany, only just over DM 1 billion were spent on such export subsidies in 1998, compared with just over DM 3 billion in 1992. By contrast, the remaining agricultural market expenditure still increased markedly. At just over DM 10 billion in 1998, it was one and a half times as high as in 1992. This pattern was mainly attributable to the growing importance of direct income support, which has increasingly taken the place of traditional intervention measures. In this connection, the most cost-intensive items by far were the farm-size-related subsidies for arable crops, which accounted for most of the market regulation spending in Germany in the last few years.

German net payment to the EU budget

Stabilisation of the net payment

Germany's weak economic growth in the last few years (compared with the EU average) and the stepping-up of Structural Fund assistance were the main reasons why the German net payment to the EU budget, which had been growing continuously up to the mid-nineties, stopped increasing as of late. This balance had initially risen noticeably, not least owing to the higher external value of the Deutsche Mark, but since 1995 it has declined quite distinctly, in fact. Last year the net payment amounted to almost DM 24 billion, or just over 0.6 % of the German GNP. Even though this was a slight increase in absolute terms compared with 1992 (DM 22 billion), it constituted a moderate reduction in terms of the economic performance, which has improved since that time. In 1994 Germany's net payment had reached its peak at DM 27 ½ billion, or just over 0.8 % of GNP.

The informative value of the net payment

However, the informative value of offsetting the national payments to the EU budget (recorded in the balance of payments statistics) against the relevant back-flows is only limited, since, *inter alia,* this calculation is subject to technical distortions. In addition, such an analysis neglects the welfare effects resulting from increasing economic integration. Finally, netting out the payment flows is vulnerable to a considerable degree of inaccuracy since a variety of classification options exist (see overview on page 65). In spite of these qualifications, the net payment to the EU budget serves as a rough measure of the financial burden caused by the Community, because, on the one hand, transfers to the Community

The debate on Germany's burden resulting from the EU budget

The Deutsche Bundesbank's balance of payments statistics capture all the financial flows between the EU and the Federal Republic of Germany and record the balance, i.e. the net payment. However, as regards the classification and inclusion of individual items, this balance has certain shortcomings which impair its informative value:

– One subject of controversy is the import charge contained in the traditional own resources, because it is not clear if it is to be assigned to those countries through which most imports reach the single European market but which are not the final destination of the imports (the "Rotterdam effect"). A similar effect on the national balance, counteracting that of the import charges, occurs with export refunds (subsidised sales of agricultural products on the world market), since they are assigned to the exporting country rather than the country of origin.

– The total expenditure of the EU budget comprises payments to third countries which cannot be assigned to individual member states. The classification of administrative expenditure poses another problem, since these costs are incurred mainly by the administrative headquarters of the European institutions, with all member states benefiting from them, however.

  If payments to third countries and administrative expenditure are deducted, the net balances of the member states do not net out. Since at least some of this expenditure would be incurred at the national level even if the EU did not exist, the countries' net payments are overestimated. For adjustment purposes, the transfers to the EU budget can be reduced in proportion to the respective country's financing share (net calculation). Assuming that the EU payments are made via the national budgets, payments to the member states may be increased in proportion to their reflux share (gross calculation).

– When analysing the payment flows in a financial year, a distinction must be made between target values and actual values. Irregular surpluses in the EU budget which do not lead to refunds or reduced contributions until the following financial year and the transfer of payment appropriations may cause major fluctuations in actual payments.

Irrespective of such adjustments, Germany is always in the group of countries with the highest net payments (measured in terms of GNP) in the Community. Only if it can be assumed that the national expenditure is refunded by the same amount of back-flows from the EU budget will a member state's net payment to the EU budget equal its fiscal net burden or net relief. However, one cannot rule out the tendency that financing at the EU level leads to higher expenditure, since the link between taxpayers and recipients of transfers is even less close and transparent than at the national level. For this reason, the analysis must also include a country's gross contribution and the pattern of total expenditure.

A frequently mentioned argument is that Germany's net financing share should be seen against the background of the unquantifiable positive effects of EU membership, such as freedom of movement and the economic advantages of free trade in the single European market. However, other member states also benefit from these advantages, and besides, there is no distinct, direct relationship between these advantages and the different national financing shares of the EU budget.

Furthermore, it is sometimes pointed out that Structural Fund assistance to other countries also leads to orders for German enterprises which involve "back-flows" to Germany. However, it must be noted that the payments to German enterprises are made for corresponding services, while Structural Fund assistance consists solely of transfers. It is acceptable to include tax revenue and employment effects resulting from these orders in Germany only if the orders are placed with enterprises which would otherwise have had unused capacities and if the project could not have been implemented without EU promotional funds.

Given the existing differences in prosperity, calls for a fair burden-sharing must not be understood as an effort by the member states to recoup the exact amount they paid in. Enhancing economic and social cohesion is one of the Community's statutory tasks. Therefore, a net transfer between the well-off and the less well-off regions is only consistent with the EU's objectives. However, a member state's relative position in terms of its economic performance should largely correspond to its relative position as a net contributor/beneficiary within the EU.

On the revenue side, the ever-increasing focus on the GNP-based own resource is giving rise to a financing system which adequately reflects the economic performance of the member states (and does not need to be adjusted). But the back-flows are distorted. For instance, the lopsided structure of EU expenditure leads to countries with a relatively small agricultural sector receiving much fewer payments than other countries.

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budget reduce the tax revenue available to the individual member states, and on the other, jointly financed expenditure relieves the national authorities at least partly of tasks they would otherwise have to carry out on their own.

Germany's net payment continues to be high

Subject to these qualifications, it should be pointed out that Germany's financial burden due to the EU budget has eased somewhat over the last few years, which has also helped to ameliorate the German current account deficit. Nonetheless, Germany is one of the EU's major net payers not only in terms of the absolute volume but also in per-capita terms or in terms of its economic performance.

Borrowing and lending by European institutions

Special borrowing authorisation ...

The EU budget does not permit expenditure to be financed through borrowing. All the same, borrowing as a financial policy instrument at the European level plays a role which should not be underrated, since certain EU institutions may take up loans within certain limits to finance lending for pre-defined purposes. Therefore, an analysis of the financial interrelationships with the Community must also include this field – not least because efforts could be made to circumvent the absence of such a borrowing authorisation in the general EU budget by increasingly using the special credit facilities.

... especially for the EIB

The European Investment Bank (EIB) is by far the most important EU institution authorised to take up loans. In 1997 this institution accounted for 97 % of the loans granted.[4] On January 1, 1999, the EIB's capital subscribed by the 15 EU member states was stepped up from € 62 billion to € 100 billion. Thus, the maximum amount of loans that may be extended pursuant to the Statute was raised from € 155 billion, which had been reached by the end of 1998, to € 250 billion.

As a matter of principle, the EIB does not provide more than 50 % of the capital required for a project. Its interest rate is composed of its refinancing costs on the capital market, which are relatively low owing to its first-class credit rating, and a margin to cover its operating costs. Hence, the EIB does not grant any open interest subsidies on its own account. All the same, borrowers profit from these loans if, due to their own low rating, they were otherwise able to borrow funds only at higher rates or not at all. Around two-thirds of the EIB's loans are designed to promote less advanced regions. For this purpose the EIB cooperates, in particular, with the Community's Regional Fund and Cohesion Fund.

Lending to German beneficiaries

Since 1992 the EIB's lending within the EU has risen steadily, from ECU 16 billion to just over ECU 25 billion in 1998. Last year loans to the tune of ECU 5.2 billion were granted to public and private borrowers in Germany, which was much more than in the preceding years (see the table on page 68). Germany's share in the EIB's total lending to the EU saw the largest increase compared with lending to

4 The European Coal and Steel Community granted slightly less than 2 ½ % of the loans. The rest were loans to some central and east European countries.

Trends of loans and borrowings in the EU

ECU billion

Item	1992	1993	1994	1995	1996	1997
Loans						
European Investment Bank 1	16.14	17.72	17.68	18.60	20.95	22.96
European Coal and Steel Community	1.49	0.92	0.67	0.40	0.28	0.54
Balance of payments 2	1.21	4.97	0.25	0.41	0.16	0.20
Euratom	–	–	0.05	–	–	–
New Community Instrument	0.01	0.03	–	–	–	–
EU, total	18.77	23.64	18.65	19.42	21.38	23.69
Borrowings						
European Investment Bank 3	12.97	14.22	14.15	12.40	17.55	23.03
European Coal and Steel Community	1.47	0.91	0.64	0.39	0.30	0.47
Balance of payments 2	1.21	4.97	0.25	0.41	0.16	0.20
Euratom	–	–	0.05	–	–	–
New Community Instrument	–	–	0.07	0.07	–	–
EU, total	15.66	20.10	15.16	13.26	18.01	23.70

Source: European Commission. — **1** Loans contracted from own resources, disregarding guarantees of the EIB vis-à-vis promoters and financial transactions from NCI resources. — **2** Financial assistance to member states, financial aid for third countries and food relief for the former USSR. — **3** Total funds raised.

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the other member states, from 10½% in 1992 to 20½% in 1998. These loans mainly went to the sectors of telecommunications, urban renewal, transport, education and health projects.[5] Almost half of the total individual loans were extended to projects in eastern Germany.

"Amsterdam Special Action Programme"

Based on the European Council's decision on growth and employment taken in Amsterdam in June 1997, the EIB drew up the "Amsterdam Special Action Programme" (ASAP). This programme is designed, *inter alia,* to furnish small and medium-sized enterprises having a high growth potential with additional venture capital. In addition, it aims at fostering investment in areas which are considered to be labour-intensive (health care, urban renewal) or to be crucial for the future (education, environmental protection and Trans-European Networks). The European Commission expects that the special programme will provide an additional lending volume of € 10 billion by the end of 2000. In a decision taken by the European Council in Cologne at the beginning of June 1999, the time limit for the ASAP was largely removed, thus creating a new permanent area of responsibility for the EIB.

5 These projects include, for instance: the installation of a new integrated fixed and mobile telecommunications network (VIAG Interkom GmbH, ECU 622.9 million); the construction of buildings at the Potsdamer Platz in the centre of Berlin (Daimler-Benz AG, ECU 354.0 million); the remodelling of 26 railway stations (Deutsche Bahn AG, ECU 229.3 million); the modernisation and renovation of hospitals in East Berlin (ECU 349.3 million) and Mecklenburg-Western Pomerania (ECU 33.4 million).

Lending operations of the European Investment Bank

ECU billion

Item	1992	1993	1994	1995	1996	1997	1998 pe
Lending operations, total (contracts signed)	17.03	19.61	19.93	21.41	23.24	26.20	29.50
of which							
in the EU	16.14	17.72	17.68	18.60	20.95	22.96	25.12
of which (by objectives) 1							
Regional development	11.79	12.46	12.04	12.14	13.81	14.65	16.59
Transport and telecommunications infrastructure	4.53	5.81	5.70	6.59	6.51	8.76	8.86
Environmental protection and quality of life	4.55	4.39	4.87	6.04	5.88	7.21	6.19
Energy	3.13	2.77	3.53	3.43	4.03	2.60	2.25
Industrial competitiveness	2.62	2.71	1.79	3.45	3.78	4.56	3.66
in the Federal Republic of Germany	1.66	2.10	2.41	2.72	3.02	3.52	5.17

Source: European Commission; European Investment Bank. — 1 Since some loans can be assigned to various objectives, the subtotals do not add up.

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Kosovo aid

Furthermore, the EIB, as part of its operations in central and eastern Europe, set up a task force to promote reconstruction in the Balkan regions affected by the Kosovo crisis. Its purpose is to meet the urgent need for assistance in this region. In this context, the EIB intends to grant so-called “soft loans”, i.e. loans at extremely low interest rates (around 1 %) and with very long maturities (30 to 40 years).

Role of interest subsidies and guarantees

The public sector budgets are only affected directly by borrowing and lending at the European level if open interest subsidies are granted or if guarantee payments must be made in the event of default. In fact, interest subsidies only play a minor role (totalling ECU 5.8 million in 1997). Indirect economic promotion occurs when borrowers, owing to their bad credit rating, would otherwise have had to pay a higher interest rate than the one they are actually being charged. This type of economic promotion affects the budget when loans turn bad and guarantee payments from public sector budgets become necessary. Most of the risk must be borne by the EIB itself and hence by its shareholders. Part of the loans are guaranteed by the EU budget. In spite of the relatively low financial risks involved in the EU institutions’ borrowing and lending transactions, caution should be exercised when stepping up these activities.

Financial Perspective, 2000 to 2006

At its meeting in Berlin at the end of March 1999, the European Council adopted the

New medium-term financial framework

financial framework of the European Union for the period from 2000 to 2006. By drawing up the Agenda 2000 in 1997, the European Commission had prepared the groundwork for this discussion. The medium-term financial framework covers both the provisions governing the Community's own resources system and the Financial Perspective which determines ceilings for the commitment appropriations of the individual policies. These ceilings must not be exceeded in the annual budgets. The Financial Perspective thus reflects the Community's political priorities.

The new Financial Perspective retains the level of maximum resources available to the Community by leaving the ceiling for the own resources at 1.27 % of GNP.[6] A key objective of the new Financial Perspective is to expand the room for manoeuvre for the current member states below the own resources ceiling by keeping the real value of major expenditure items largely constant. This is how the costs of pre-accession aid and the accession of new member states can be financed.

Agricultural policy resources

Totalling almost € 300 billion,[7] the Common Agricultural Policy remains the largest expenditure item. However, its share is to be reduced to an average of just over 42 % (see the chart on page 70 and the table on page 72). This reduction will even be somewhat sharper than these figures suggest, since some of the rural renewal measures which had formerly been financed by structural policy are now booked under agricultural policy. For the current planning period (1993 to 1999) a share of roughly 47 % was envisaged for agricultural policy.

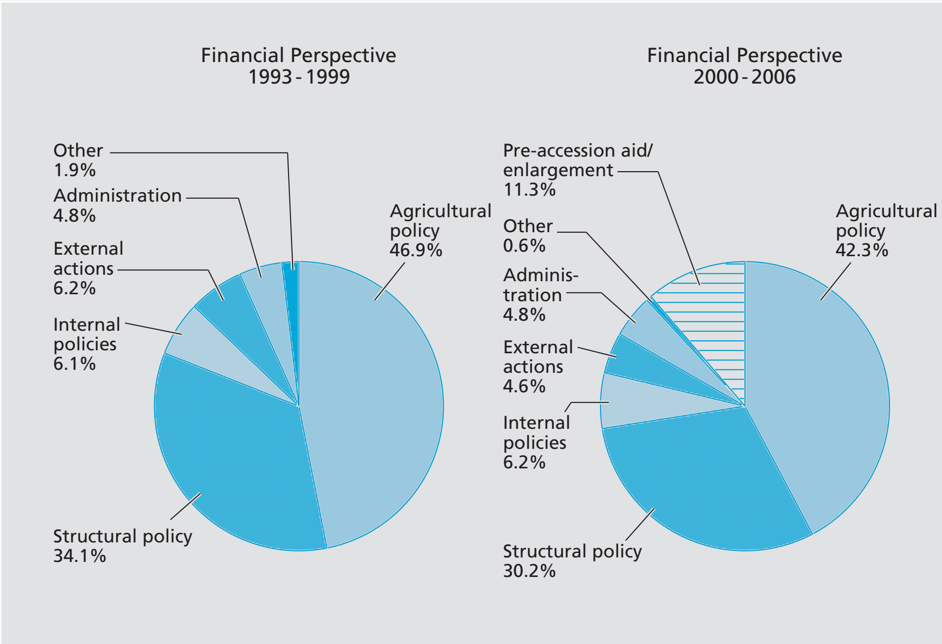
Agricultural market decisions

Since the agricultural subsidy systems have led to sizeable overproduction, lasting reforms in this sector are necessary for spending to be restricted effectively. The recently adopted measures are mainly limited to a continuation of the trends set by the agricultural market reform in 1992 pointing in the direction of direct compensation payments instead of traditional price support. However, guaranteed prices will now be lowered less sharply and will take effect much later than proposed by the Commission. For instance, the progressive reduction by a total of 15 % for milk and milk powder will not set in before the 2005-6 marketing year, whereas the Commission had suggested it should start in the 2000-1 marketing year. The milk quota scheme will be prolonged up to the end of the medium-term financial planning period, and the quotas will even be increased. However, for cereals and beef the gradual price cuts will already set in from 2000-1. As a financial compensation for these price reductions, more direct aid is to be granted.

It was not possible to implement more comprehensive reform proposals such as a proportional contribution by the national budgets to the financing of direct aid for farmers (co-financing) or the option of limiting or gradually reducing payments to individ-

6 In fact, expenditure growth had not reached the ceiling in the current planning period. On average, only nine-tenths of the ceiling was actually utilised.
7 All the amounts specified in euro in the context of the Financial Perspective are expressed as values at constant 1999 prices.

Structure of the Community budget



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ual agricultural enterprises. If these proposals had been implemented, the subsidies would have taken the form of a more personal guarantee of the basic income in agriculture. Instead, the direct income support granted under the present system is closely linked to output (i.e. to the cultivated land and the reference yield of cereals); hence, its amount mainly depends on the farm size.

Plans regarding the Structural Funds

After a strong expansion in the nineties, the Structural Funds are now to be maintained at the current level of promotion expenditure. € 195 billion, or 28 % of the commitment resources, have been envisaged for the Structural Funds in the planning period. Technically, the number of objectives promoted through Structural Fund assistance will be reduced from seven to three, but this does not involve a corresponding reduction in the total number of projects being promoted.[8] Instead the funds are being increasingly channelled to regions with structural adjustment difficulties. No less than 6 % of the Structural Fund assistance is designed to facilitate the process of transition in regions which will fail to meet the eligibility criteria in future. In this sector, the member states negotiated a number of special provisions for their relevant regions.

Continuation of the Cohesion Fund

In 1993 the Structural Funds were supplemented by the Cohesion Fund in order to facilitate the economic catching-up process and the preparation for monetary union through special means in the four economic-

8 The promotion of Objective 1 regions continues to be by far the largest item, accounting for roughly two-thirds of Structural Fund assistance.

ally least advanced member states (Spain, Portugal, Greece and Ireland). In spite of their progress in convergence, the Fund has continued to exist even after the start of monetary union. In the planning period, € 18 billion have been envisaged for this fund – a share which is only slightly lower than the amount allocated to it before. In 2003 it will be assessed whether Cohesion Fund assistance should be reduced once a beneficiary country reaches a per-capita GNP of over 90 % of the EU average. However, the Council of Ministers can object to granting Cohesion Fund assistance to new projects, in principle, if the member state in question has violated the provisions of the European Stability and Growth Pact.

Resources for new member states

More than 11 % of the commitment appropriations have been envisaged for future and new member states of the Union, including almost € 22 billion for pre-accession aid. In addition, the appropriations for the new member states in the traditional expenditure categories (agricultural policy, structural policy, administration and other policy areas) amount to € 58 billion. This allocation is based on the working hypothesis that the candidates for accession[9] will enter the EU starting in 2002. Spending in the current EU member states and on the enlarged Union (EU-21) is strictly separated, so that a delayed accession should not lead to means being redirected to finance expenditure in the EU-15 countries.

Impact on Germany

For Germany this will mean a change in both payments to the EU budget and back-flows. As regards financing, the share of the GNP own resource is to grow further at the expense of the VAT own resource, which will result in an even closer link between contributions and the national economic performance.[10] This should result in relief – albeit moderate. A greater impact is to be expected from the reduction of the German financing share for the United Kingdom's rebate.[11] Towards the end of the planning period, the two aforementioned effects will lead to an annual relief of around € 700 million for Germany.

As regards payments out of the EU budget, Germany can count on an increasing share in the total Structural Fund assistance owing to the restructuring of these funds. Regions in eastern Germany will receive more funds thanks to the allocation ratio for Objective 1 regions. In spite of the reduction in the number of eligible regions, on the whole the old Länder will benefit from stepped-up promotion resulting from the fact that the eligibility criteria are more favourable for Germany. This mainly applies to promotion schemes in the framework of the new Objective 3, which primarily focuses on the adjustment and modernisation of employment, education and vocational training policies.

9 Hungary, Poland, the Czech Republic, Slovenia, Estonia and Cyprus.
10 The maximum call-in rate of the value-added tax base currently amounting to 1.0 % will be reduced to 0.75 % in 2002 and further to 0.5 % in 2004. The GNP own resource will rise accordingly to cover the remaining financial requirements.
11 As a rule, the UK correction mechanism is financed by the other member states in relation to their GNP shares. However, Germany's share was limited to two-thirds of this amount before and will now be reduced further to one-quarter.

Financial Perspective for the EU budget, 2000 to 2006

€ billion, at 1999 prices

Item	2000	2001	2002	2003	2004	2005	2006	Total
Agricultural policy	40.9	42.8	43.9	43.8	42.8	41.9	41.7	297.7
Structural policy	32.0	31.5	30.9	30.3	29.6	29.6	29.2	213.0
Internal policies	5.9	6.0	6.2	6.3	6.4	6.5	6.6	43.8
External actions	4.6	4.6	4.6	4.6	4.6	4.6	4.6	32.1
Administrative expenditure	4.6	4.6	4.7	4.8	4.9	5.0	5.1	33.7
Reserves 1	0.9	0.9	0.7	0.4	0.4	0.4	0.4	4.1
Pre-accession aid for candidate countries	3.1	3.1	3.1	3.1	3.1	3.1	3.1	21.8
Enlargement	–	–	6.5	9.0	11.6	14.2	16.8	58.1
Commitment appropriations	92.0	93.5	100.4	102.2	103.3	105.3	107.4	704.3
Payment appropriations	89.6	91.1	98.4	101.6	100.8	101.6	103.8	686.9
of which for enlargement	–	–	4.1	6.7	8.9	11.4	14.2	45.4
Payment appropriations in % of GNP 2	1.13	1.12	1.14	1.15	1.11	1.09	1.09	.

1 At the prices of the year in question. — **2** Up to 2001: EU-15, from 2002: EU-21.

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Initial estimates by the Federal Government suggest that the above-mentioned decisions could reduce Germany's net payment from just under 0.6 % of GNP in 1999 to just over 0.4 % in 2006. In absolute terms, it would remain relatively close to its current level. Since relief regarding the own resources will only take effect in 2002 and there are still some outstanding payment appropriations from the financial planning period ending on December 31, 1999, the rise in both gross and net payments is likely to continue – at least in the next few years.

The EU budget in monetary union

The future development of the Community budget is also relevant to European monetary union. The Stability and Growth Pact requires the countries participating in monetary union to conduct a national financial policy which ensures a sustainable financial situation. This could fuel efforts to transfer national tasks to the European level and to introduce recourse to credit financing in the EU budget. Other proposals call for a new source of financing to be autonomously determined by the Union ("EU taxes"). Steps in this direction might lead to unwelcome fiscal developments at the European level.

Problems associated with a structural growth of the Community budget

Current resources suffice

For the time being, new and unavoidable Community-wide tasks can be financed within the limits of the existing own resources ceiling, particularly if the potential unleashed by the dismantling of subsidies granted out of the EU budget is exploited. In agricultural policy, such measures which go beyond the results of the recent decisions are feasible, in principle. It should also be noted that the total economic costs of agricultural policy far exceed the subsidies recorded in public sector budgets.[12]

The rapid abolition of price support would enhance further liberalisation on the world market. In addition, such a stance is also likely to ease the financial strains which will be caused by integrating the candidate countries into the subsidy system of the Common Agricultural Policy. Furthermore, an ongoing review of the Structural Funds remains a key financial policy task at the European level. Just like subsidies, such assistance facilities tend to become self-perpetuating even after the original reasons for granting assistance have been eliminated. This is evidenced by the fact that Cohesion Fund assistance is still being paid even though the beneficiary countries have become members of monetary union.

Requirement of fiscal discipline also applies to the EU

As regards the national fiscal policies of the countries participating in monetary union, sustainable public finances should be achieved, in particular, through compliance with the provisions of the Stability and Growth Pact. This would not only facilitate the job of monetary policy but would also improve the conditions for growth and employment in the Union. Although the EU's supranational budget is not officially subject to these provisions, it is a part of the Community's government sector and hence also plays a role in achieving the fiscal objectives set by the Community. Against this background, it would be problematic, for instance, to introduce the option of credit financing in the EU budget, particularly if efforts are being made to balance the national budgets. Furthermore, the national efforts to reduce government spending should not be thwarted by a counteracting trend at the supranational level. These requirements also call for strict limits on the expenditure envisaged in the EU budget and, in particular, a close monitoring of the allocation of funds.

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12 Taking into account the additional costs consumers have to pay owing to unduly high food prices, the economic burden on the European Union caused by agricultural policy is estimated at 1.4% of GDP for 1998. See: OECD, Agricultural Policies in OECD Countries, Paris, 1999.