The EU budget and its financing: looking back and ahead

The EU budget is the joint budget of the European Union (EU) Member States. It has so far amounted to roughly 1% of the gross national income of the EU. The budget is financed by contributions from the Member States (own resources). There is no provision for extensive debt financing. The Member States' returns reflect the EU's policy priorities. By far the largest part of the budget is allocated to agricultural and cohesion policy. Agricultural policy focuses on bolstering the income of farmers. The aim of cohesion policy is to promote economic convergence within the EU. Funds are therefore channelled primarily into economically weaker Member States. A smaller amount of spending is dedicated to areas with a more pronounced pan-European focus. These areas include internal and external security, international cooperation and development aid, the environment and research.

The multiannual financial framework for 2021 to 2027 is currently being prepared. Negotiations are proving difficult. Amongst other things, the funding gap created by Brexit has to be plugged. Moreover, the EU budget is expected to help meet the European climate targets. On top of this, there is the recent coronavirus pandemic, which is posing an exceptional challenge for the Member States and the EU. In relation to the EU budget, the pandemic has mainly led to stabilisation measures which are simply a temporary addition to the regular framework. This article discusses the measures that have already been agreed. However, it focuses on the structure of the EU budget to date and the reform debate, leaving aside more recent events.

On the revenue side of the EU budget, the Member States' contributions are largely based on economic size. Its financing is fairly complex and opaque, however. In order to change this, the rebate system could be made much simpler and the VAT-based own resource, which is subject to complicated rules, could be replaced by resources linked to gross national income. At least some of the revenue from common European instruments which target EU-wide environmental impacts, such as the EU Emissions Trading System, could flow to the EU budget.

The EU budget is used mainly on the expenditure side to redistribute funds between the Member States. This hinges on the varying returns from agricultural and cohesion policy. On the whole, the negotiation process is cumbersome and is often dominated by the Member States' consideration of their own net contribution. This tends to be to the detriment of expenditure with a stronger European focus. One option worth considering might be to separate the aspects of redistribution and support for economically weaker regions more distinctly from the programme areas of the EU budget. This could potentially lead to a more targeted debate about what spending should occur at the European level.

The negotiations to date have indicated that the "Brexit gap" is likely to be closed on both the revenue and expenditure side. Germany has signalled that, as a strong economic performer, it is willing to make higher net contributions. One particular issue that remains unresolved at present is the extent to which measures to contain the coronavirus crisis should be taken via the EU budget.

The multiannual financial framework of the EU budget: an overview

Preliminary remarks

This article describes the EU budget and its financing, both looking back over past planning periods and looking ahead to its future design. At present, the coronavirus pandemic is confronting the EU and its Member States with huge challenges. The health of the general population is the central concern, and extensive measures to contain and manage the pandemic are being taken to protect it. This is occurring primarily at the national level, but EU-wide cooperation is also increasingly taking shape. Furthermore, there is intense debate as to how the Member States and the EU as a whole should respond to the economic impact of the pandemic. The EU budget will also be involved in crisis resolution. So far, the measures adopted are mainly a temporary addition to the regular framework. The outcome of the debate remains to be seen. This article describes measures adopted thus far in connection with the coronavirus pandemic (see pp. 47 to 49). However, it does not discuss the economic implications of the pandemic and possible measures to manage them in future plans. It focuses on the current structure of the EU budget and on reforms that are under discussion, leaving aside recent events.

Multiannual financial framework determines broad lines of EU budgetary policy

The EU budget is the joint budget of the EU Member States. The multiannual financial framework (MFF) specifies its spending structure, maximum size and type of financing. It usually spans a period of seven years and forms the framework for the annual budget plans during that time. The Council of the European Union adopts the MFF on the basis of a European Commission proposal, after obtaining the consent of the European Parliament. The current MFF is for 2014 to 2020.

MFF marks out own resources ceiling

The EU budget's revenue is almost exclusively contributed by the Member States in the form of "own resources". There is no provision for extensive debt financing.[1] The types of own resources and the ceiling are first agreed at the EU level and then ratified by the national parliaments. The ceiling is defined in relation to the gross national income (GNI[2]) of the EU Member States[3] and is currently set at 1.20%. The own resources ceiling is normally much higher than the annual expenditure ceilings. This allows the EU to meet its payment commitments, even in the event of an unexpected economic downturn, say. In addition, there is a certain amount of scope to mobilise additional expenditure over and above the annual expenditure ceilings in the face of unforeseen circumstances, without impinging on the own resources ceiling.[4] Finally, this is a way to make provision for risks in connection with the EU's lending.

Payment appropriations and commitment appropriations budgeted on the expenditure side

On the expenditure side, the MFF lays down commitment appropriations and payment appropriations.[5] Commitment appropriations indicate the maximum amount of the legal commitments that may be made each year. In the current MFF, they are limited to an average of 1.02% of EU GNI per year. Payment appropriations represent the expected actual payments that the EU makes in a year. These payments, in turn, stem from legal commitments (commitment appropriations) from the current and pre-

1 The EU can, on a limited scale and for specific purposes, raise funds on the capital market and pass them on to individual countries as loans. The European Commission publishes an annual overview of borrowing and lending activities as an annex to its Financial Report. For the latest figures, see European Commission (2019a), pp. 79-82.
2 GNI was defined as the reference variable for the EU budget. It differs from gross domestic product (GDP) by including the balance of primary income payable and receivable by residents. GNI thus encompasses the entire income of all residents, regardless of whether it was generated domestically or abroad. The difference between a country's GNI and GDP is generally small, but in Ireland and Luxembourg GDP is much higher than GNI.
3 The United Kingdom is still counted as an EU Member State in this article, unless otherwise stated.
4 In the current MFF, the "margin for unforeseen expenditure" instrument can be used for this.
5 The ceilings for commitment and payment appropriations are fixed in absolute euro amounts. They increase in a given year by the unused funds from the previous year. If GNI developments are not as expected, the ceiling in billion euro continues to apply. This results in a changed ceiling as a percentage of GNI. The European Commission reports these technical adjustments in the annex to its annual Financial Report.

Measures in the EU budget in connection with the coronavirus pandemic

The coronavirus pandemic is having a major impact on the Member States of the EU, prompting European bodies to adopt decisions and measures in an array of areas – some of them designed to mitigate the economic repercussions. These steps include extraordinary measures relating to the EU budget, which this report is focusing on. In addition to the resolutions already adopted in April 2020, further decisions have been mooted but are yet to be firmed up. There is a high degree of uncertainty surrounding the precise extent to which the pandemic will impair economic development. It is also unclear how the effects will be distributed over time and from a regional perspective.

Measures as part of the current budget

In March 2020, the European Commission launched the Coronavirus Response Investment Initiative (CRII). Its centrepiece is to allow Member States to retain unspent cohesion policy pre-financing, which represents a departure from the normal rules and gives the countries concerned access to additional liquidity totalling €8 billion.[1] Furthermore, fund resources can now be provided more swiftly. Available resources from the structural and investment funds can be used to respond to the coronavirus crisis in many different ways. One of the new aspects is the ability to provide small and medium-sized enterprises with working capital support. The European Commission anticipates that a total of €37 billion from these funds will be used under the initiative. In addition, the European Commission has made arrangements to expand the Solidarity Fund to encompass public health emergencies. This unlocks up to €800 million in the current year for Member States particularly hard hit by the pandemic. Other changes allow financial resources from the European Globalisation Adjustment Fund to be used for coronavirus-specific purposes. The intention is for these resources to be used to support individuals who have lost their job and self-employed people who find themselves in financial difficulties.

At the beginning of April, the European Commission launched further concrete programmes for the current fiscal year and made amendments, for example, to the European Maritime and Fisheries Fund. It also increased the liquidity and flexibility of cohesion policy and further reduced the applicable administrative constraints (CRII+). These modifications enable crisis-related measures under the cohesion policy framework to be 100% EU-funded, meaning that no national co-financing is necessary. It will also be possible to transfer resources between the different cohesion policy funds, i.e. the structure of the EU budget can deviate from the original plan. In addition, resources destined for specific regions of one country can be redirected to other regions within that country, and expenditure can be focused on a small number of regions. This is to account for the fact that measures to tackle the coronavirus pandemic are not necessarily most urgently needed in the economically weakest regions.

A further coronavirus-specific measure will see €1 billion from the EU budget being provided as a guarantee to the European Investment Fund, with the aim of increasing incentives for banks to grant credit to busi-

1 This measure concerns the following four funds: the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund.

nesses. The European Commission anticipates that the guarantee will mobilise some €8 billion in financing for at least 100,000 small and medium-sized enterprises in the EU. The EU budget is able to unlock the guarantee by deferring longer-term projects of the European Fund for Strategic Investment (EFSI).

Using a variety of budgetary operations, all funds still available under the current financial framework are being reallocated, ultimately unlocking an additional €3 billion in the current budget for financing coronavirus-related expenditure. For example, the Emergency Support Instrument is being reactivated and its scope of application broadened. This is to be funded by mobilising the Flexibility Instrument and exhausting the Global Margin for Commitments. In addition, more of the Contingency Margin is to be used than had previously been planned.

All in all, tackling the coronavirus pandemic represents the top priority in the final year of the current financial framework (2020). As things currently stand, the upper limits of the current financial framework remain unchanged, but a far greater portion of the planned resources will likely be called on than without these measures (entailing commensurately higher national contributions).

Measures concerning future planning periods

The financial framework for 2021 to 2027 is currently under discussion. It is not affected by the measures described above. However, the European Commission has announced that it will earmark considerable funds in the next framework for the purposes of curbing the economic repercussions of the pandemic.

Also related to the EU budget, the European Commission has proposed the temporary aid instrument SURE, which the Eurogroup has endorsed. The idea behind SURE is to swiftly provide EU countries with financial assistance of up to €100 billion in the form of low interest loans. These can be used to finance actual or expected expenses related to maintaining employment during the coronavirus crisis (e.g. short-time work schemes). Countries making use of this borrowing facility will not be required to comply with any additional conditions; they will simply be expected – like all Member States – to respect the recommendations of the European Semester. In order to finance the loans, the European Commission will borrow on the capital market in the name of the EU. The EU countries are backing these loans by providing guarantees for 25% of the total credit amount (i.e. up to €25 billion). The size of a Member State's guarantee contribution is to be decided on the basis of the proportion of EU GDP that it accounts for. This would see Germany committing around €6 billion for interest and principal payments. In addition, the loans are to be backed by future EU budgets, again underpinned by each Member State with its respective funding share. These guarantees mean that highly favourable interest conditions are to be expected. These will be passed on to the countries receiving the loans.

SURE is a new borrowing option at European level. It is limited in both duration and scope. Should any country be unable to service its assistance loans and the guarantees of the EU countries prove insufficient to cover this, future EU budgets would be placed under a fiscal burden. For this reason, buffers would need to be built into future EU budgets. These will consist of an appropriately large margin between the own resources ceiling and the payment ap-

propriations ceiling. This buffer would enable interest and principal payments on bonds to be met without the need for reallocation of EU budgetary resources. SURE is to be constructed such that the annual interest and principal payments do not exceed €10 billion.

Besides this, the buffer would have to be large enough to cover the risks arising from the EU's other borrowing options as well as the guarantees from the EU budget. In addition to SURE, the existing balance of payments assistance facility for non-euro area countries is also to be used as a way of providing those countries with loans to assist them in dealing with the coronavirus crisis. Like SURE, this coronavirus-related support will probably also be granted without the imposition of additional conditions, whereas, in the past, use of the facility has always involved economic and fiscal policy agreements.[2]

How the EU level should respond to the coronavirus pandemic in the various policy areas is currently the subject of intensive discussions. One possibility is for resources for crisis management to be planned into the EU budget in the next financial framework. This could involve reducing other expenses or (temporarily) scaling up Member States' contributions to the EU budget. However, ideas for taking on mutualised debt at the European level on a very comprehensive scale and, in some cases, also on a more permanent basis in future – potentially through recourse to an innovative new financing instrument – have also been put forward. This would entail substantive change for the financial relationships within the EU, though. In the EU and the euro area, responsibility for fiscal and economic policy still lies, in large part, at the national level. A crucial point would be for the same set of shoulders to bear responsibility for fiscal and economic policy and the liability for any risk arising therefrom. Should a fundamental shift at the European level prove desirable or be considered indispensable, this should consequently be transparently and legally anchored in a major step towards further integration.

2 Euro area countries can apply for ESM credit lines. These are also financed through mutualised debt. However, since the ESM rests on an intergovernmental agreement, it does not give rise to a contingent liability for the EU budget.

vious years. In the current MFF, payment appropriations are budgeted at an average of 0.96% of EU GNI per year, and are therefore lower than commitment appropriations, as is normally the case. One reason for this is that some of the commitments made are only paid out in subsequent years, when GNI has generally risen. Thus, for this expenditure, the budgeted payment appropriations as a percentage of GNI can be lower than the commitment appropriations that were originally budgeted. Additionally, the scope for commitment appropriations normally is not fully exhausted.

EU budget much smaller than sum of national budgets

The EU budget has so far amounted to around 1% of EU GNI annually (around €160 billion). By contrast, government spending at the level of the Member States is considerably higher, at around 45% of EU GNI. This reflects the heavily decentralised fiscal policy approach in the EU.

Brexit requires adjustments against current MFF

Negotiations on the MFF for 2021 to 2027 have already been ongoing for some time.[6] It is being prepared for just 27 countries now, as the United Kingdom withdrew from the EU on 31 January 2020. The United Kingdom was a net contributor, meaning that it contributed more to financing the EU budget than it received in return (for more on the implications of Brexit for the EU budget, see the box on pp. 51 and 52).[7] This has to be factored into the new MFF – by way of higher revenue from the remaining Member States or lower spending.

Negotiations still ongoing

The European Commission originally proposed an average annual commitment ceiling of 1.11% of EU27 GNI for the next MFF.[8] Of this, 0.03 percentage point is allocated to the European Development Fund, which is to form part of the EU budget under this proposal. Adjusted for the Fund, the proposed commitment ceiling is 1.08%. The potential payments to the EU27 would thus be slightly lower than those envisaged for the EU27 in the current MFF (around 1.13% of EU27 GNI). The loss of the United Kingdom's net contributions would therefore be compensated for on both the expenditure and revenue side. The negotiations to date have featured countervailing calls for a larger EU budget and calls for a stronger limit. It remains to be seen how the current coronavirus pandemic will affect the continuing negotiations. The European Commission has announced a new proposal on the next MFF, which is to contain measures to overcome the economic impact of the pandemic. The "European Green Deal" announced by the Commission is also likely to be reflected in it. The Deal calls for at least 25% of budget funds to contribute to climate objectives.

EU budget revenue

Status quo

Financing via contributions of EU Member States …

The EU budget has just a few of its own revenue sources and is funded primarily by contributions from the Member States. The planned annual revenue has to cover the planned expenditure. Differences that arise during implementation of the budget are carried over to the budget plan for the next year in an amending budget.

… and primarily based on GNI

The EU budget draws its revenue predominantly from traditional own resources, the value added tax (VAT)-based own resource and the GNI-based own resource.[9] Their relative weight remained broadly unchanged between 2007 and 2018 (see the chart on p. 53). Traditional

6 The European Commission presented a first draft of the next MFF in May 2018. Since then, two revised drafts have followed, first from the Finnish Presidency of the Council in December 2019 and then from European Council President Michel in February 2020. The Commission announced a new proposal in response to the coronavirus pandemic, which was not yet available as this report went to press. This article discusses the original Commission proposal.
7 The United Kingdom's net contribution (incl. customs duties and administrative expenditure) on average between 2014 and 2018 was just under €10 billion per year or 0.08% of the EU27's GNI.
8 See European Commission (2018a).
9 Of relatively minor importance is revenue from the European competition authorities, e.g. from anti-trust penalties or fines for Member States which failed to meet the deadline for transposing EU law into national law. The same is true of contributions agreed with non-EU Member States.

Rules governing the EU budget in the Withdrawal Agreement with the United Kingdom

The United Kingdom left the European Union (EU) on 31 January 2020. The Withdrawal Agreement provides a transition period until 31 December 2020. Union law still predominantly applies in the United Kingdom during this period. In addition, it is agreed that both the United Kingdom and the EU will honour all financial obligations undertaken while the United Kingdom was a member of the EU.

Thus, the United Kingdom will continue to participate in the EU budget until the end of the current multiannual financial framework (end of 2020), as previously arranged. By contrast, the next financial framework for 2021 to 2027 will be drawn up for the remaining 27 EU Member States. The United Kingdom will be able to participate in EU programmes in future just like other non-EU countries.[1] In this case, the United Kingdom would have to make a financial contribution to the EU budget. The contribution amount and the scope of the cooperation would be negotiated separately.

The Withdrawal Agreement sets out in detail how mutual obligations shall be fulfilled following the end of the transition period. The bulk of these obligations stem from "RAL" (from the French "reste à liquider"). RAL are appropriations committed that have not yet been paid. They are created when multi-annual projects are financed, such as the building of a bridge. According to the European Commission's projections, RAL will stand at around €300 billion at the end of 2020.[2] Usually these funds would be almost fully paid out over the course of the next financial framework and only a small proportion de-committed.[3] The Withdrawal Agreement stipulates that the United Kingdom shall be liable for its share of RAL and further commitments in the amount of its financing share in the current financial framework that is still ongoing. Its share would be around 12%.[4] In line with this, the United Kingdom would still have to make a gross payment of approximately €35 billion for RAL by the end of 2027. This corresponds to an annual average of roughly 0.2% of its gross national income (GNI) in 2019, with the largest share likely to be due within the first few years.[5] Furthermore, the United Kingdom contributes to payments in connection with pension entitlements of EU employees and contingent liabilities that were entered into during its time as a Member State.[6] In return, the United Kingdom receives retroactive EU budget revenue proportional to its financing share (e.g. from fines which were legally imposed before 2021 or for the enforcement of which legal proceedings were opened before 2021). Since the "UK rebate" is paid out in the year after it is calculated,

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1 In particular, the other members of the European Economic Area (EEA) – Iceland, Norway and Liechtenstein – and Switzerland have thus far made use of this option. For instance, Norway is involved in the EU's cohesion policy and in selected EU programmes such as Erasmus, Galileo and Horizon 2020.
2 See European Commission (2019b).
3 In the current financial framework, 50% of RAL from the previous financial framework was called on in the first two years and over 80% in the first three years. The European Commission expected an almost complete reduction by the end of 2019. See European Commission (2019b), p. 2.
4 This was the United Kingdom's average own resources share between 2014 and 2018.
5 The European Commission expects that only €6 billion of RAL will be de-committed by 2024. See European Commission (2019b), p. 3. Part of the RAL (roughly 4%) is likely to result from projects in the United Kingdom, meaning that EU payments also flow back there. Thus, in net terms, the United Kingdom's average annual RAL spending would come to roughly 0.14% of its 2019 GNI.
6 While no details are known, payment burdens from pension obligations are considerably lower than those from RAL. Darvas (2019) estimates that they will total €4 billion for the United Kingdom up until 2027.

the United Kingdom will also receive around €5 billion in 2021 (0.2% of UK GNI in 2019). In particular, the burdens from contingent liabilities and the revenue shares from fines cannot be reliably estimated. This is one reason why the exact level of payments between the United Kingdom and the EU is still unknown.

Under the terms of the Withdrawal Agreement, the transition period can be extended once by up to two years. The United Kingdom would have to apply for an extension before 1 July 2020. In addition, the extension would have to be decided by common accord between the EU and the United Kingdom. In this case, the United Kingdom's access to the EU single market would also be extended. It is envisaged that the United Kingdom would then pay contributions to the EU budget to compensate for this.[7] The amount of these contributions would have to be negotiated with the extension. The next financial framework for the EU would be drawn up without the United Kingdom regardless of a potential extension.

7 Currently, there is also such a rule for non-EU countries which belong to the EEA. Their contributions to the EU budget are set out in the EEA agreement of 1994.

own resources had a share of roughly one-seventh in total revenue. They mainly consist of uniform EU-wide customs duties on imports to the single market. The Member States collecting the customs duties retain a portion, which serves as flat-rate compensation for the costs of collection.[10] Only traditional own resources stem from an original EU policy field, the EU Customs Union. The other types of resources, on the other hand, are financing contributions which the Member States make from their respective budgets. The VAT-based own resource is based on a harmonised VAT tax base. It likewise made up around one-seventh of EU revenue in the aforementioned period. The most important revenue item, accounting for five-sevenths, is based on the GNI of each Member State. The annual financing needs determine the contribution rate for the GNI-based own resource, meaning that the EU budget is balanced at the planning stage and the specified ceilings are adhered to.

Correction mechanisms aim to prevent excessive burdens on individual countries

On the revenue side, a complex system of rebates limits the financial burden on individual Member States which receive relatively low returns from the EU budget. On balance, this is currently providing relief for the United Kingdom, the Netherlands, Sweden and Germany.[11] The "UK rebate" is the most well-known and, at just over 0.2% of UK GNI, also the largest rebate. The flat-rate reimbursement of customs collection costs is relatively large for the Netherlands and Belgium because of their sizeable ports.[12] However, the administrative expense is likely to be less significant given higher customs

10 In the current MFF, the flat-rate percentage of collection costs retained is 20% of customs revenue. In the previous MFF it was 25%.
11 All other things being equal, rebates for individual Member States increase the general GNI-based own resource, which all countries contribute on a pro rata basis. Denmark and Austria are also receiving rebates under the current MFF, but these are smaller than the payments to finance the rebates for the other countries.
12 In 2018 the flat-rate compensation for collection costs in Belgium and the Netherlands amounted to 0.11% and 0.08% of national GNI, respectively, compared with an EU average of 0.03% of EU GNI.

revenue. Therefore, the global compensation for collection costs is sometimes also seen as a hidden rebate for these countries.[13]

Reform debate

Discussion of simplified VAT-based own resource and new own resources

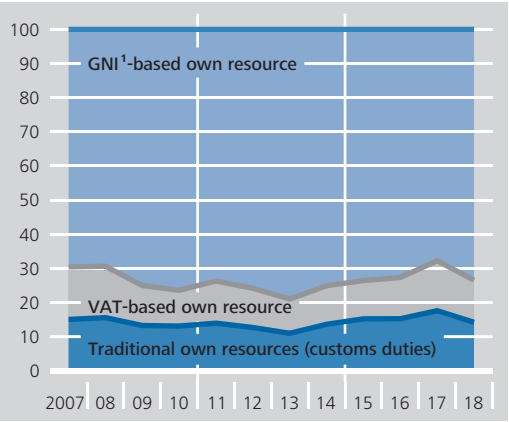
In its proposal for the next MFF, the European Commission suggests changing the system of own resources. It proposes a simpler method of calculating the VAT-based own resource. At present, this own resource is based on a special tax base which harmonises the various national definitions.[14] The calculations are complex, and collection is an administrative burden. In future, the European Commission wishes to use a simpler method of deriving the VAT-based own resource from national tax revenue and standard tax rates.[15] For the sake of simplicity, it assumes that the tax bases and tax rates have a similar structure in the individual countries. Furthermore, the European Commission proposes tapping new revenue sources making up a total of 12% of the EU budget. To do so, it is bringing two environmental taxes into play: 20% of national revenue from the EU Emissions Trading System and a new joint tax on non-recycled plastic. It also cites the financial transactions tax and the digital services tax as two other new European taxes which could be contributed (in part) to the EU budget in future. In addition, the Commission is proposing an EU corporate tax coming to 3% of a common consolidated corporate tax base.[16] However, this would require the EU Member States to first harmonise the national tax bases for corporate tax. Additional revenue sources such as these would mean that less GNI-based own resources would be required.

Elimination of rebates also under discussion

In addition, the European Commission is proposing that all rebates be eliminated and that the flat-rate compensation for collection costs for traditional own resources be halved to 10%. The UK rebate ends with the withdrawal of the United Kingdom from the EU in any case. The European Commission wishes to phase out the remaining rebates over a five-year period, to ensure that the net burden on the affected countries increases only gradually.

Funding structure of the EU budget

%



Sources: European Commission and Bundesbank calculations.
1 Gross national income.
Deutsche Bundesbank

GNI-based own resource links financing to economic strength

GNI-based contributions are based directly on an indicator of Member States' economic performance. This makes them a suitable revenue source for the EU budget where financing is to factor in the Member States' varying levels of economic strength. One option that could be considered in order to simplify the system of own resources is replacing the VAT-based own resource entirely with GNI-based own resources. The European Commission proposal to reform the VAT-based own resource would simplify the present calculation method, but the level of the VAT-based own resource would then depend on the structure of national tax rates and tax bases. It would thus be less geared towards economic strength. This would also give Member States opportunities to de-

13 See, for example, Darvas, Mazza and Midos (2019), p. 9 and European Commission (2018b), p. 18.
14 The tax base is also limited to 50% of national GNI, the intention being to avoid putting an excessive strain on countries with a comparatively high share of consumption.
15 See European Commission (2018b), pp. 20 ff.
16 The proposed new types of own resources are not "real" EU taxes that are decided and levied by the EU. This would require a Treaty change, and the necessary unanimity currently does not appear to exist. The High-Level Group on Own Resources established by the European Commission considers this kind of EU tax desirable, but is not proposing such a tax under the present conditions. See High-Level Group on Own Resources (2016), p. 24.

sign their VAT in a way that reduces their contribution.[17]

Customs duties clearly related to EU

Other proposed types of own resource that are less dependent on GNI have a weaker link to Member States' economic strength. They should therefore have a clear European connection where possible. Customs duties are an ideal example. EU customs duties are levied on imports into the EU Customs Union and cannot be allocated to individual countries within the single market. One option that could be considered is to move away from deriving collection costs as a fixed percentage of customs revenue. Instead, the costs could be gauged and reimbursed more specifically where possible. This would eliminate potentially hidden rebates, and would boost the transparency of the EU budget.

New own resources linked to EU policies

Common European environmental levies can also have a European aspect to them. This is the case, in particular, if the environmental pollution has an EU-wide impact and is not merely of regional or local importance. This applies to the EU Emissions Trading System, for example. It would thus be fairly plausible to transfer the revenue from this, at least on a pro rata basis, to the EU budget.

More transparent rebates

Finally, the system of rebates is currently very complex and makes the financing of the EU budget opaque. However, rebates could still be necessary in future to achieve political agreement, for example to avoid high net contributions by individual countries. In this case, making the rebate system simpler and more transparent would be a welcome move. Harmonised and generally applicable criteria for rebates would help here.[18]

EU budget expenditure

Status quo

Agricultural policy absorbs most EU budget funds

In the current MFF, the EU budget comprises six overarching areas of expenditure (for the names and composition over time, see the table on p. 55). Agricultural policy accounts for the largest share, at 39% (see the chart on p. 56). The vast majority of this expenditure (just under three-quarters) serves primarily to safeguard farmers' income. It constitutes direct payments based on area size, and measures to support agricultural markets (for the sake of simplicity, both will be referred to together as direct payments in the remainder of this text). The remaining portion of agricultural expenditure goes towards agricultural policy environmental and research payments. These funds promote regional environmental policy measures as well as research, development and competitiveness in the agricultural sector.

Cohesion is second most important expenditure category

The second largest expenditure item is cohesion policy (34%), which aims to promote economic, social and territorial cohesion in the EU. To this end, support is given to a wide range of project-based measures.[19] In most cases, the Member States must also make a financial contribution to the projects. The largest portion of cohesion funds flows to countries and regions whose economic performance is much lower than the EU average (see the chart on p. 57).[20]

17 For example, Member States could reduce their VAT-based own resource without decreasing national tax revenue. To do this, they would have to raise the standard tax rate while reducing the associated tax base. The higher standard tax rate would lower the common tax base calculated according to the Commission's new method. This is because the Commission's method assumes a uniform share of the tax revenue resulting from the standard tax rate.

18 In a 2004 report, the European Commission discussed ceilings on the net amount relative to GNI and per capita GNI, for instance. See European Commission (2004), pp. 28 ff.

19 In the current MFF, the cohesion funds are being used to pursue 11 defined objectives to promote growth. These include: 1) objectives to enhance competitiveness, e.g. support for small and medium-sized enterprises; 2) environmental objectives such as promoting sustainable mobility; 3) social objectives such as combatting poverty and discrimination.

20 Cohesion funds are largely disbursed via three funds: the European Regional Development Fund, the European Social Fund and the Cohesion Fund. The criteria for the granting of cohesion funds are defined in the MFF. Resources from the first two funds are currently linked to the regions' GDP per inhabitant (measured in purchasing power standards). By contrast, Cohesion Fund resources are granted based on the Member States' GNI per inhabitant (in purchasing power standards). This must be lower than 90% of the EU average.

Name and allocation of areas of expenditure in individual Financial Frameworks (MFFs)

	Name in …		
Name in this report	2007-13 MFF	2014-20 MFF	2021-27 MFF[1]
Agricultural policy of which: Direct payments Residual: agricultural policy environmental and research payments	2. Preservation and management of natural resources of which: Market-related expenditure and direct payments	2. Sustainable growth: natural resources of which: Market-related expenditure and direct payments	3. Natural resources and environment of which: Market-related expenditure and direct payments
Cohesion policy	1b. Cohesion for growth and employment	1b. Economic, social and territorial cohesion	2. Cohesion and values[2,3]
Research and infrastructure	1a. Competitiveness for growth and employment	1a. Competitiveness for growth and jobs	1. Single market, innovation and digital[4]
Administration	5. Administration	5. Administration	7. European public administration
External action	4. The EU as a global player	4. Global Europe	6. Neighbourhood and the world[5]
Security and citizenship	3. Citizenship	3. Security and citizenship	4. Migration and border management 5. Security and defence[6]
Compensatory payments	6. Compensations	6. Compensations[7]	

1 According to European Commission proposal of May 2018. **2** Including €30 billion for "Erasmus+" (previously in Research and infrastructure). **3** Including €24 billion for the new instrument "Economic and Monetary Union", which includes the Structural Reform Support Programme (budget for the euro area). **4** Including €9 billion for the new instrument "Digital Europe". **5** Including €35 billion for the "European Development Fund", which so far has not formed part of the EU budget. **6** Including €13 billion for the new instrument "European Defence Fund". **7** Compensatory payments are disregarded due to their small size (0.1% of the EU budget's total expenditure for 2007-13 and 0.03% for 2014-20) and because they are granted only temporarily. They ensure that new EU Member States receive more from the EU budget than they pay in during their first few years of membership.

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However, 15% of the cohesion funds are earmarked for regions whose per capita GDP is above the EU average.

Other expenditure categories of lesser importance

Additionally, expenditure on research and infrastructure projects of pan-European importance plays a role (13%). This includes support for research and innovation as well as spending on the expansion of European transportation, energy and digital networks. This is followed by the categories of administration and external action (6% each). External action includes spending on humanitarian aid or development aid, for example. The remaining expenditure (2%) is allocated to security and citizenship measures, which includes spending on border control, immigration, asylum policy, healthcare and consumer protection, amongst other things.

Spending priorities slowly changing

Compared with the previous MFF (2007 to 2013), the spending structure of the current EU budget is not radically different (see the chart on p. 56). However, there has been a shift away from agricultural and cohesion policy (-4 and -2 percentage points, respectively) and towards research and infrastructure (+5 percentage points).

Reform debate

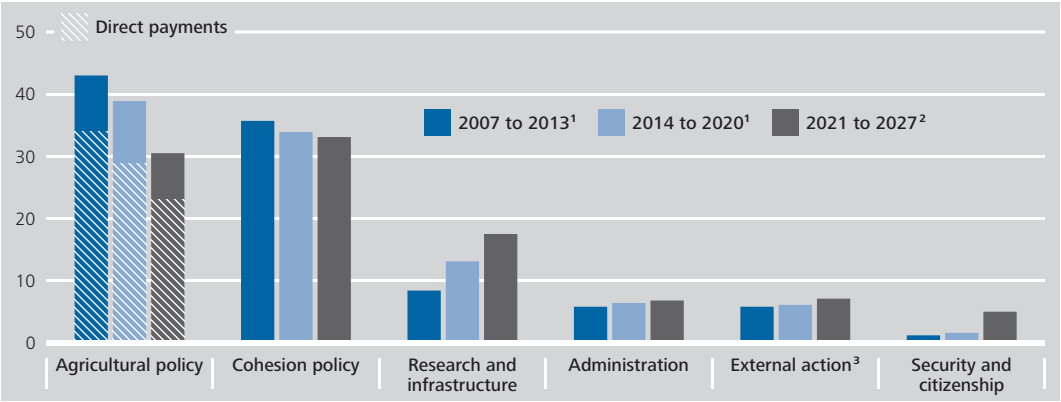
EU budget for European tasks

The EU has a decentralised design and is based on the principle of subsidiarity. This prescribes that government tasks and the associated expenditure are decentralised wherever possible. In this way, differing preferences in the provision of public goods, say, can be better taken into account. However, there are benefits to undertaking some spending jointly. This is sometimes referred to as European added value to spending.[21] It can arise because a public service can be rendered more cheaply when it is provided jointly. This kind of added value can

21 See, inter alia, Fuest and Pisani-Ferry (2019).

Use of EU funds by area of expenditure

Percentage shares



Sources: European Commission and Bundesbank calculations. **1** Planned commitment appropriations. **2** Funds for commitment appropriations according to the European Commission proposal of May 2018. **3** To aid comparability, the European Development Fund is also excluded from the 2021 to 2027 data.

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also be created, in particular, when spending has a cross-border impact. It can (ideally) have positive effects across Europe (e.g. reducing environmental damage). In addition, a common budget can be used to support catching-up processes or for redistribution among Member States.

Areas of responsibility with a European focus

It is not always possible to clearly determine the areas in which it is beneficial for spending to be undertaken jointly, and the division of responsibilities is ultimately a political decision. A number of factors tend to speak in favour of joint funding in the following areas of responsibility:

- The administrative activities of the European Union serve all Member States, meaning that it is not only the Member States in receipt of the spending which reap the benefits. This is an argument that supports joint financing. Administrative expenditure mainly comprises the staffing and operating costs of the various EU authorities.

- Development aid, asylum and immigration policy are other areas in which the EU might benefit from pursuing a joint strategy. Citizens generally have a right to freedom of movement within the EU. It therefore seems important to optimise coordination in these areas.

- Defence policy and super-regional environmental measures (such as those aimed at $C0_2$ emissions reduction or water conservation) can also be considered European tasks, as the benefits of such measures extend far beyond the Member State that adopts them. However, this is not the case for environmental policy measures per se. Measures to reduce local fine particle pollution, say, should therefore be taken at the regional or local level instead – possibly on the basis of a common regulation with minimum standards.

- Basic research projects can benefit people throughout the whole of Europe. Besides this, cost advantages can arise when efforts are pooled. At the same time, this is bound to be of most benefit to countries in which the funds are spent, because expenditure on research can significantly enhance a region's reputation and have positive repercussions for the surrounding areas.

- Cross-border infrastructure networks are also likely to benefit all the Member States involved. It may therefore be worth taking a coordinated approach to expanding them

and, depending on the scope of the action, financing them jointly.

Joint European objectives can also be achieved through coordinated rules

The examples listed above show that joint tasks generally make sense in areas that have an impact far beyond the national borders of the countries involved. However, in some cases, a binding EU framework may also be enough to coordinate the efforts of the Member States. Examples of this are the limits on levels of nitrates in drinking water or of nitrogen oxide in the air. In other cases, a suitable alternative would be for individual countries to cooperate if, for instance, they were the countries most strongly impacted by external effects.

Agricultural policy focused on safeguarding income

In the two major spending blocks of agricultural and cohesion policy, the focus is likely to be less on the joint provision of a European public good in the above sense. On the whole, agricultural policy consists of direct payments which are mainly used to safeguard farmers' income.[22] The EU's agricultural policy is a controversial topic overall.[23] Only around one-quarter of agricultural spending is allocated to agricultural policy environmental and research payments.

Main aim of cohesion policy to promote growth in economically weak regions

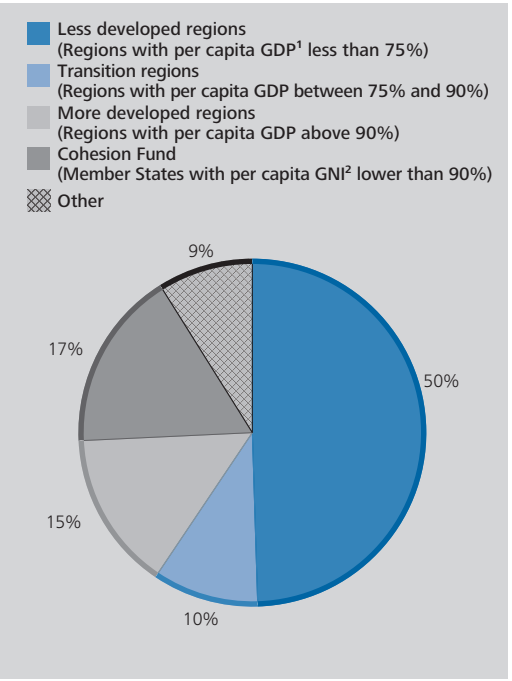
The aim of cohesion policy is to even out economic disparities within the EU. To this end, funding is given to projects that aim to promote growth. Most of the funding flows to regions which are economically weaker in terms of per capita income. As a result, cohesion policy displays elements of redistribution between Member States of differing economic strengths. At the same time, the funding is specifically intended to help the economic catching-up process. The scope of the redistribution is ultimately a political decision. In this context, economic convergence between Member States is a shared European objective.

Effectiveness of cohesion policy is disputed

However, empirical studies reach very different conclusions regarding the growth-enhancing effects of the EU's cohesion policy.[24] A small number of studies identify positive long-term growth effects. Others find only a short-term positive effect. But a large number of studies conclude that there is no (or even negative) correlation between the incentive measures and growth in the recipient Member States. The results vary depending on factors such as region, type of investment, and institutional conditions in the individual Member States.[25] Most studies agree that cohesion policy contributes rather little to economic convergence.

In the debate about the next MFF, some are calling for a significant strengthening of the

Planned use of cohesion funds in the 2014-20 Financial Framework*



Sources: European Commission and Bundesbank calculations. * Percentages relate to the EU average. **1** Gross domestic product. **2** Gross national income.
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22 Although direct payments are conditional on compliance with environmental restrictions (cross-compliance), compliance with these legal requirements is mandatory in any event. They are therefore flat-rate payments rather than compensation for additional environmental efforts. See, inter alia, Heinemann and Weiss (2018).
23 For example, the European Court of Auditors is critical of the European Commission's proposals to reform the common agricultural policy after 2020. One particular point of criticism is that direct payments will not help achieve the desired environmental and climate goals. See European Court of Auditors (2018).
24 See Darvas, Mazza and Midoes (2019).
25 See Crescenzi and Giua (2019).

New MFF: stronger focus on European added value

policy areas with greater European added value. The European Commission has also formulated this objective.[26] To achieve it whilst keeping the size of the EU budget the same, spending on agricultural and cohesion policies would have to be reduced. Although the current proposals envisage fairly sizeable shifts in this regard, they do not amount to a fundamental reorientation. In the Commission's proposal, the share of the two spending categories of direct payments and cohesion policy[27] is down by just under 7 percentage points (see the chart on p. 56). The largest part of this cut is to direct payments, amounting to 6 percentage points. Nonetheless, at 56%, these two largest spending categories still clearly dominate. The area of research and infrastructure is intended to receive the strongest boost. In addition, the share of spending on security and citizenship is set to rise from 2% to 5%.

Additional euro area budget to support reform and investment

Within the spending area of cohesion policy, the European Commission is proposing, for the first time, a separate budget instrument specifically for the euro area countries. It would amount to around €17 billion, or 1.3% of the total budget of the next MFF. The Eurogroup agreed on the key points in December 2019. The new Budgetary Instrument for Convergence and Competitiveness (BICC) is aimed at supporting the reforms and investment in the euro area that have been recommended within the framework of the European Semester. The Council of Ministers emphasises that the BICC will be a flexible instrument and that this is what primarily differentiates it from other EU budget programmes, whose objectives are set for seven years. Countries that do not participate in the BICC[28] are to receive return flows from the Convergence and Reform Instrument (CRI) as compensation. However, the exact structure of the new instruments has not yet been determined.

Financial links with the Member States

Development of payment flows with Germany

Germany's financial contribution stable

In the first five years of the current MFF (2014 to 2018), Germany's payments to the EU budget averaged 0.85% of Germany's GNI, or €27 billion per year (see the chart on p. 59).[29] As a percentage of GNI, they were thus as high as in the first five years of the previous MFF. Over the previous budget period as a whole, however, the payments amounted to 0.89% of GNI per year because they had risen sharply in the last two years of the period. The reason for this rise was that expenditure on longer-term projects within the framework of cohesion policy is usually called on towards the end of the MFF period, in particular.[30] Payments by the Member States to the EU budget then rise in line with this expenditure. A perceptible increase such as this would also have been expected in 2019. However, Germany's payments to the EU budget indicate that the volume of cohesion funding collected last year did not increase.[31] Nonetheless, significantly higher payments to the EU budget are to be expected in

26 See European Commission (2018c).
27 For better comparability with the current MFF, the EU programme Erasmus+ has been assigned to the category "Research and infrastructure" in this analysis. In the European Commission's proposal for the next MFF, however, it is assigned to the category "Cohesion and values", which also comprises traditional cohesion policy.
28 Countries that participate in the current exchange rate mechanism (ERM II) may decide to join the BICC.
29 In this section, traditional own resources and administrative expenditure, which are excluded from the European comparison of payment flows in this report, are also factored in.
30 Funding that is not collected during a budget year can be carried over to the next year. However, as a rule, it must be called on by the end of the third year for which it was intended, at the latest. Otherwise, the funds expire automatically (N+3 rule). In the previous MFF, by contrast, the funds had to be called on after two years at the latest (N+2 rule). For the next MFF, the European Commission is aiming to return to the N+2 rule. It is also possible to carry unused funds over to the first years of a new MFF. As a result, payments are also sometimes slightly higher in the first few years of an MFF.
31 The European Commission has not yet published the figures for 2019. However, at just under €30 billion, payments to the EU budget are also likely to have amounted to around 0.85% of Germany's GNI.

Germany's financial links with the EU budget

As a percentage of gross national income

Sources: European Commission and Bundesbank calculations. **1** VAT-based own resource and GNI-based own resource (including corrections) as well as customs duties. **2** Including administrative spending.

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2020, mainly owing to the coronavirus pandemic (see the box on pp. 47 to 49).

Specific structural features of Germany's financing contribution

The share of traditional own resources in Germany's payments to the EU budget, at 14%, corresponds to the average across all EU countries (2007 to 2018). However, the two other types of own resources that make up Germany's financial contribution display special features. This is primarily due to the fact that the VAT call rate applicable to Germany is just half the usual rate.[32] This means that the share of the VAT-based own resource (7%) is significantly lower than the EU-wide figure (12%). The weighting of the GNI-based own resource (including the UK rebate) is correspondingly higher (79% as opposed to 73%).

Funds returning to Germany lower

Within a multiannual financial framework, return flows from the EU budget to Germany fluctuate less strongly than payments to the EU budget. Compared to the last MFF, they have fallen. Having previously stood at 0.45% of GNI per year (both on average over the first five years as well as over the period as a whole), they have so far averaged 0.35% (€11 billion) per year in the current MFF. The decline was particularly pronounced for direct payments and cohesion policy (see the chart on p. 60). In the case of cohesion policy, the relatively good economic performance of Germany's eastern federal states played a role.[33]

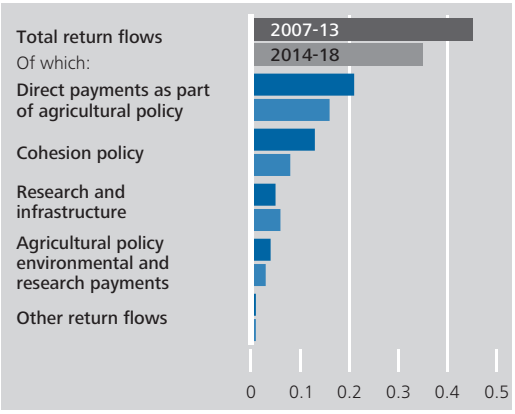
Higher net contributions from Germany on balance

On balance, Germany's net payments rose slightly in the current MFF. Having amounted to 0.44% of GNI in the previous MFF, they averaged 0.50% of GNI (€16 billion) per year in the first five years. They are likely to have reached this level in 2019, too. A significant increase is expected in 2020, given the additional spending in connection with the coronavirus pandemic.

32 Instead of the usual call rate of 0.30%, a rate of 0.15% applies to Germany. This is one of two rebates granted to Germany, the other being that Germany only pays 25% of its actual funding share of the UK rebate. It is therefore referred to as the "rebate on the UK rebate".
33 See Federal Ministry of Finance (2013), p. 48.

Return flows from the EU budget to Germany by expenditure category

As a percentage of gross national income



Sources: European Commission and Bundesbank calculations.
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Europe-wide payment flows

Only moderate differences in financing contributions in relation to GNI

In the overview of the financial links of all Member States to the EU budget, both payments and return flows are adjusted in order to improve comparability.[34] In the following, traditional own resources are thus excluded from the payments to the EU budget. Owing to their large ports, the Netherlands and Belgium record particularly high customs revenue (known as the "Rotterdam effect" and the "Antwerp effect"), which they transfer to the EU budget. However, as a result of the single market and tariff-free trade within the EU, this revenue is mainly attributable to products that are destined for other Member States. With that in mind, customs duties transfers to the EU budget should not be attributed to individual countries.[35] Excluding customs duties, payments to the EU budget in 2018 stood at around 0.8% of national GNI (see the chart on p. 61). Owing to the UK rebate, payments by the United Kingdom were the lowest, at just under 0.6% of the country's GNI. The Netherlands, Sweden and Germany also received rebates, meaning that their financing contributions were comparatively low in relation to their GNI.[36] Payments by the other Member States deviated less from the average across all other EU countries.

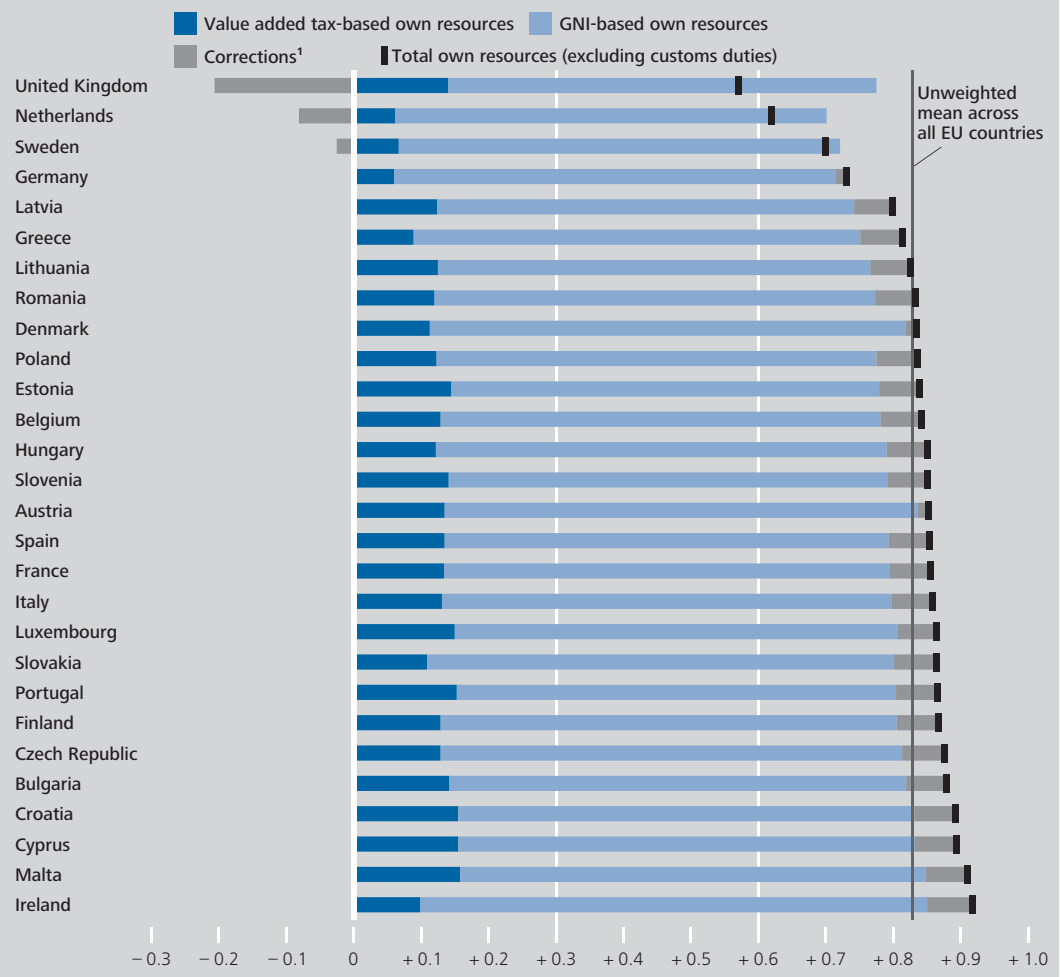
Greater variation in return flows to Member States

When comparing return flows from the EU budget to the Member States, only the operating expenditure is taken into account. This means that administrative expenditure is not factored in. The latter is incurred in Belgium and Luxembourg, in particular, because the European institutions have their headquarters there. When the return flows from the EU budget are adjusted in this manner, the differences between the Member States are larger than for payments to the EU budget (see the chart on p. 62). As an (unweighted) average across all countries, the return flows amounted to 1.8% of national GNI in 2018. The United Kingdom received the smallest return flows, at less than 0.3% of its GNI, while Hungary received the largest at 5%. The countries with a rebate listed above generally record rather small return flows. Large return flows are received in particular by countries that only joined the EU later on. This is partly because the largest differences stem from the return flows from cohesion policy and these countries are undergoing an economic catching-up process. As a share of GNI, return flows from cohesion policy ranged from 0.02% in the Netherlands and Denmark to 3.5% in Hungary. However, this difference was also considerable for direct payments under agricultural policy, at 1.45 percentage point (0.05% in Malta and 1.5% in Bulgaria). Owing to far lower expenditure overall, differences in the return flows for agricultural policy environmental and research payments and the remaining expenditure are much smaller (0.7 and 0.5 percentage point).

34 The figures presented for Germany in the section above are altered slightly by these adjustments. Traditional own resources averaged 0.13% of GNI per year for the period 2014 to 2018, while administrative expenditure amounted to 0.01% of GNI per year in the same period. In this analysis, Germany's net contribution is therefore just over 0.1 percentage point lower on average over the years 2014 to 2018, amounting to 0.4% of GNI per year.
35 The flat-rate reimbursement of the collection costs is also excluded. This means that the effect sometimes described as the hidden rebate to the Netherlands and Belgium is not reflected in the payment flows considered here.
36 The order is different for per-capita payments to the EU. In this case, Germany's payments were higher than the EU-wide average, at €305 per capita compared with €238 per capita.

Value added tax-based and GNI*-based own resources, as well as corrections

As a percentage of national GNI, 2018



Sources: European Commission and Bundesbank calculations. * Gross national income. **1** The corrections include the UK rebate, the gross reductions for the Netherlands, Sweden and Denmark, and their funding by the other countries. Germany, the Netherlands and Sweden only contribute ¼ of their actual financing share of the UK rebate. The VAT call rate is also halved for these three countries, meaning that their contributions to the value added tax-based own resources are half as large as usual. This rebate is funded by all countries through higher GNI-based own resources and is not presented separately.

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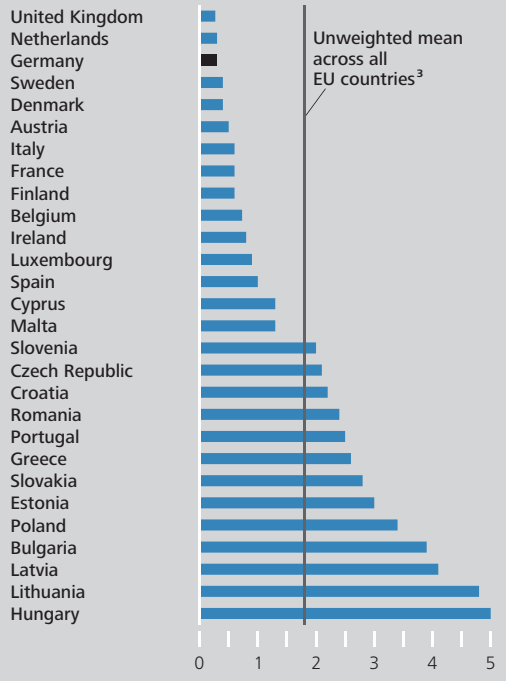
European Commission reports operating budgetary balances

The European Commission reports operating budgetary balances for the individual Member States. These indicate whether countries receive net payments from the EU budget (net recipients) or make net payments to the EU budget (net contributors).[37] On average over the first 5 years of the current MFF, 10 of the 28 EU Member States were net contributors (see the chart on p. 63). At 0.4% of its GNI, Germany's net payments were the highest, followed by the net payments made by Sweden and the Netherlands. 18 countries were net recipients. Net return flows to Hungary, Bulgaria and Lithuania amounted to over 3% of these countries' respective GNI.

37 A number of conversions are made in order to calculate the operating budgetary balances. For instance, the VAT and GNI-based own resources of a Member State are adjusted so that, firstly, the funding shares of the Member States remains the same and, secondly, the sum of the national contributions (VAT and GNI-based own resources) corresponds to the sum of the operating expenditure. After that, the respective VAT and GNI-based own resources are deducted from the operating expenditure. This allows the balance of customs duties and administrative expenditure to be attributed to the Member States in proportion to their GNI. As a result, the operating budgetary balances of all EU countries add up to zero. In terms of amount, they differ slightly from the net contribution derived by calculating the difference between operating expenditure and own resources excluding customs duties. However, the net contribution positions of the Member States are the same. See European Commission (2019a), pp. 73 ff.

Return flows from the EU budget

As a percentage of national GNI,[1] operating expenditure[2] 2018



Sources: European Commission and Bundesbank calculations. **1** Gross national income. **2** Expenditure excluding administrative expenditure. **3** Factoring in the countries' different sizes, the weighted mean amounted to 0.8% of EU GNI.

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Net contributions mirror financial links …

The reporting of net contributions to the EU budget or operating budgetary balances is a controversial topic. Some rightly note that the net contributions should not be equated with the advantages or disadvantages of EU membership.[38] Certain calculation steps are likewise contentious. Nonetheless, the net contributions illustrate the financial links to the EU budget and provide a rough idea of the redistribution between the Member States that takes place within it. This is certainly a relevant aspect in terms of analysing the EU budget, which appears to justify the reporting of these figures.

… and are roughly oriented to economic strength

Looking at redistribution, it is clear that there is a link between the net contribution of a country and the strength of its economy. In the period under review, weaker economic performance tended to go hand in hand with a smaller net contribution. This becomes clear if the per capita net contributions of the countries are viewed in relation to their economic strength – as measured by per capita GNI, for example (see the chart on p. 64). However, there were also some individual deviations, at least when viewed from this perspective. For instance, the return flows for Bulgaria and Romania were small given their economic performance. On the other hand, there were countries whose net payments (per capita) were smaller than those of countries with a lower GNI per capita (such as Ireland or Luxembourg).

Allocation issues a major factor in negotiations

The net contribution plays a role in negotiations on the EU budget because issues relating to the allocation of funds have a high political weight. Governments therefore regularly push for expenditure that flows to their respective country in disproportionately large measure compared to their respective funding share (especially agricultural policy and cohesion policy funding). These elements tend to push spending on matters with a stronger European focus into the background. To overcome this, some propose a stronger separation between the decision about redistribution in the EU budget and the debate regarding the content of the budget.[39] It might therefore be worth considering whether redistribution issues should be negotiated separately, for example. Whether this would increase the Member States' willingness to finance more joint European public goods remains to be seen. Agreeing on how redistribution between the Member States should take place is probably no easy task, either. But it could potentially help make the debate about the spending structure more focused.

Looking ahead

Size of EU budget will probably increase

The negotiations that have taken place up to now on the MFF for 2021 to 2027 have indicated that the EU budget will increase some-

38 See, for example, European Parliament (2020a) or High Level Group on Own Resources (2016), p. 61.
39 See, for example, Pisani-Ferry (2020) or European Parliament (2020b).

what in relation to GNI. The European Commission's new proposal in response to the coronavirus pandemic will probably exceed this by quite some way. It is to contain additional funding to help cushion the economic impact of the pandemic. Climate action could also be made a higher priority. At the same time, the United Kingdom's withdrawal from the EU means the loss of a large net contributor. To close the funding gap this will leave, the remaining EU countries need to make higher payments or reduce the level of spending in the EU budget. Germany's annual net contribution is expected to rise in comparison to the last few years. Even before the outbreak of the coronavirus pandemic, the Federal Government announced that Germany, with its strong economy, would be prepared to pay a higher contribution.

Funding to remain geared to economic strength

GNI-based own resources are likely to constitute the majority of the payments to the EU budget in future. The EU budget will thus continue to be funded largely in proportion to the economic strength of the individual Member States. Any new types of own resources should be well justified and have Europe-wide relevance, as is the case for receipts from European emissions trading, for instance. Regardless of this, the own resources system could be simplified, for example by replacing the complex VAT-based own resources with GNI-based own resources. Any rebates should be more transparent and easier to understand.

Stronger focus on expenditure with European added value

The European Commission is aiming to boost expenditure in areas with high European added value. It recently reaffirmed its intention to focus in particular on promoting climate action in the EU budget by announcing the European Green Deal. If the overall size of the EU budget is to remain the same, a significant increase in these expenditure items is only possible if cuts are made in other areas of spending. The European Commission's original proposal certainly outlines a perceptible shift in this regard. However, more than half of the expenditure is still earmarked for direct payments to farmers and

Operating budgetary balances*

As a percentage of national GNI,[1] average for the period 2014-18

Sources: European Commission and Bundesbank calculations. * Excluding administrative expenditure and traditional own resources (customs duties). **1** Gross national income.

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cohesion policy. The debate on how to fund the additional spending in relation to managing the coronavirus crisis has only just begun (see the box on pp. 47 to 49).

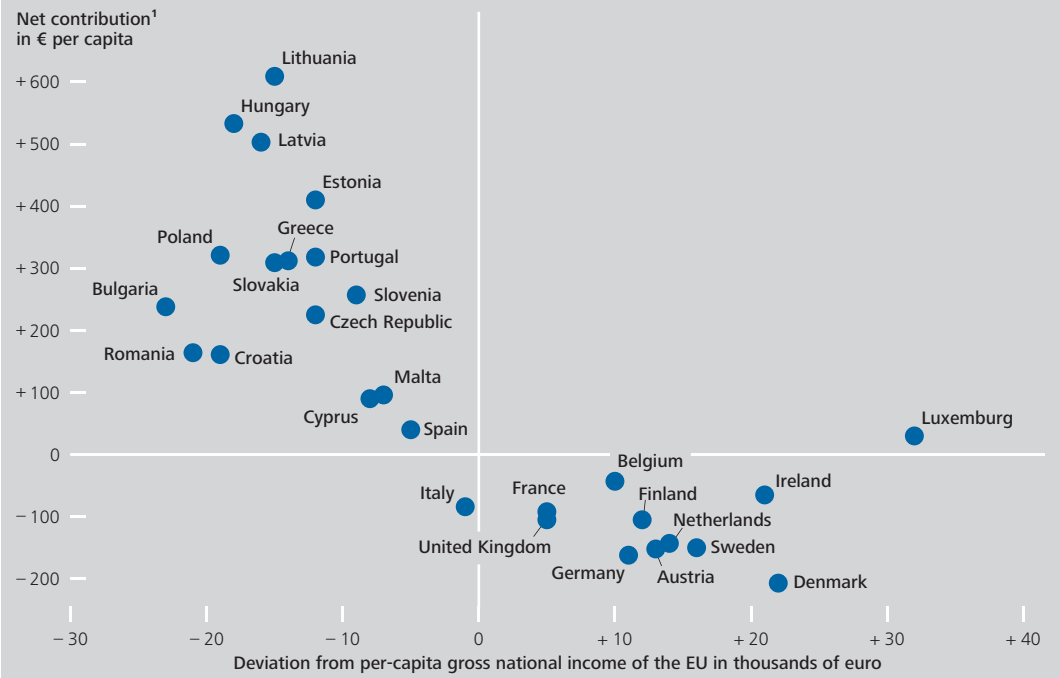
Redistribution determined by spending structure

The EU budget is used to redistribute funds between the Member States. This tends to involve the flow of funds from stronger economies to weaker ones. The net contributions to the EU budget roughly reflect this. Redistribution is based mainly on the spending structure of the EU budget – especially the differences in return flows in the context of agricultural and cohesion policy. The latter, in particular, is intended to facilitate economic convergence. However, according to empirical studies, it is uncertain whether this aim is achieved.

Disentangle the negotiation process

On the whole, the EU budget negotiation process is cumbersome and is often dominated by the Member States' consideration of their own net contribution. One option worth exploring might be to negotiate redistribution issues sep-

Net contributions to the EU budget and economic strength of the EU Member States in 2018



Sources: European Commission and Bundesbank calculations. **1** Countries with positive per-capita contributions are net recipients, countries with negative per-capita contributions are net contributors. Excluding administrative expenditure and traditional own resources (customs duties).
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arately, thus systematically removing them from the debate about a suitable spending structure. The debate about the EU budget would then potentially concentrate more closely on tasks with a Europe-wide focus.

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