Spending at EU level saves at national level … and more

How does the EU budget 'save' Member States' MONEY?

The European Union (EU) budget is often portrayed as a cost for net contributors to the EU, and it is revealing how redistribution to other Member States is presented as having little value for contributing states. Conversely, while critical of a number of areas of expenditure, the academic literature generally considers the EU budget to be far too small to contribute effectively to the demands made upon it. Studies of the optimum distribution of competences and finance, following the theories of fiscal federalism, call for a considerable expansion of the EU budget and competences.

There is no doubt that there are many ways to improve and expand the EU budget based on comparisons with federal states. However, as the EU is not a federal state, it does not have the capacity to rearrange its competences in this way (the EU Treaty is hard to amend), and any proposal for change would have to remain within the EU's Treaty limitations. The EU's supranational nature, bringing sovereign nations together voluntarily in a complex single market that requires some pooling of competences, makes it a unique budgetary entity. Reality therefore complicates explanations of the EU budget, the value it adds and the consequent savings for Member States, based on the following constraints:

- The EU is not a federal state and the budget is far from alignment with fiscal federalist theories of an ideal distribution of competences;
- The European Union has very few competences and a small budget;
- A large share of the EU budget is dedicated to supporting the single market and integration and 'compensating' for their impact. For this reason, the biggest budgetary items are transfers destined for cohesion and agricultural policy. These transfers are difficult to identify as savings, but they nevertheless contribute to building and sustaining the architecture of the EU and the single market, which considerably reduces the costs of cross border business operations;
- For a large part, the EU budget works as an incentive, co-financing investments in EU objectives.

It is important to stress that it is very counterproductive to see the budget solely as a tool to seek savings for “Member States", which is associated with reducing the annual budgetary cost to national treasuries. While paying less to the EU budget may be a punctual ‘saving’ for the treasury on a given year, the consequences may actually be forfeited returns from common investment and common action in the future.

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The social, economic and environmental state of the member states are closely interlinked (with or without EU membership). Curtailing the EU budget in areas of common needs and objectives may lead to have subsequent higher costs to the treasuries or lead to missed future revenues from higher economic returns. In fact, no federal or international budget has been designed with the objective to save funding of the contributors. The objectives are of higher order, to reach agreements and create value for all members.

Nevertheless, the EU budget through common action with pooled resources can and does bring savings to the member states. This briefing will explore the following areas:

a) Areas where the EU budget either saves costs for the Member States directly;
b) Areas where the EU budget saves budgetary costs for Member States indirectly;
c) Improvements that can create more ‘savings’ and create more added value.

**How the EU budget saves costs**

These are the kind of savings that the EU budget is capable of providing:

- Reductions due to efficiencies of scale through collaboration and coordination;
- Savings for net EU contribution recipients in achieving more onerous EU standards, which they could or would not have applied without EU membership and support. This reduces the effort needed for net contributors to persuade countries to follow a particular policy path, and is important in such potentially expensive policy areas as climate change mitigation, for example.
- A reduction in administration in areas of central competence, replacing 27 (ex-28) structures.

Studies of fiscal federalism consider the EU budget too modest to achieve the potential gains of further joint financing and developments of scale.

A study by ECORYS\(^2\) identified areas where the EU could achieve more with the same resources by greater pooling of its finances (or ‘spending less to achieve the same’ – which represents a saving). These areas were related to ensuring common standards, enhancing the internal market and creating positive economic spillovers due to larger markets. The existence of a customs union is also considered essential to the functioning of the single market. Greater investment to deepen the internal market is seen as a very effective way to save money on several fronts and to enhance benefits. Tax and customs coordination save the EU considerable costs. The EU budget pays these through the national retention of a share of customs receipts from the duties collected, and the costs of common borders and customs are considered to be much lower than separate arrangements. The benefits incurred by the free movement of goods are wide, but nevertheless require a common set of product safety and health standards, which has led to the existence of single coordinating agencies, reducing costs in comparison with running multiple national bodies that perform similar tasks using different standards and procedures. For example, product testing for compliance with compulsory common EU standards in one Member State eliminates the need for retesting in other Member States.

EU policies on border control, security and defence, which are relatively limited to date, nevertheless demonstrate great potential for expansion, with possible savings in terms of returns on investment. While advances are being made, there is further scope for expansion, and the consequences of underinvestment in this area were witnessed during the migration crisis.

Another area where considerable savings could be made is in common EU consumer protection policies and the agencies necessary to execute them. However, potential savings are missed in the lack of further collaboration on health (beyond the savings created by the European Medicines Agency). Health structures and services coordination could be improved to provide increased returns from common investment.
More controversial are the costs generated by operations of the common agricultural policy. While the absence of a common agricultural policy would not lead automatically to any savings, as this would depend on the replacement chosen by the Member States (considering they would likely try to protect the sector from the impact of other Member States’ agricultural support policies). With an easy calculation, it is possible to see that 3/4 of the contributed funds actually return to the contributing country, only approximately 25% of the cost of the cap is a real transfer. Contrary to other funds, the contributions the policy and the redistributed funds are from central government budget back to the central government budget (of the Ministry of Agriculture), not directly to the farmers or to other beneficiaries like regional authorities. Without changing the policy, it would be possible to reduce the cost of the EU budget by 30 billion, even though it would not change the tax burden.

The ‘savings’ element of regional policy is more complex to assess. After multiple reforms of EU regional policy and the increasing conditionalities imposed, expenditures can no longer be considered as a transfer in the sole interest of the beneficiary. While net recipients are financial beneficiaries of the EU budget, expenditure is tightly linked to EU objectives and standards. Poorer countries in particular avoid some of the onerous costs of the European Union acquis. It is important to highlight that many EU environmental and safety standards were designed by EU net contributors. Such high standards are unlikely those that would be chosen by countries with a lower GDP per capita, and therefore there is a rationale behind providing budgetary assistance. This is all the more apparent today, with new proposals on an energy transition and environmental objectives presented in the new EU green deal, European Structural and Investment Funds (ESI Funds) spending will have to be further aligned. More advanced in these areas, net contributors support many of those objectives, while poorer Member States often see such goals as being beyond their financial capacity. The ESI Funds provide considerable benefits in terms of reaching structured agreements and may not only facilitate agreements, but also reduce the costs of achieving the objectives compared with bilateral agreements (which would be unlikely to achieve the same results).

Finally, the European Fund for Strategic Investments (EFSI), or InvestEU in the future, is another area where savings and economies of scale are particularly important. The debt and guarantee instruments at EU level offered through European Fund for Strategic Investments (EFSI) and other financial instruments supported the EU budget, bring down the risk premiums and the costs of capital. This allows for public goods operations to be financed more cheaply compared to the use of grants.

These instruments also play an important role in mainstreaming EU objectives into investments, such as ‘climate proofing’. Projects which under normal lending conditions would not be able to offer high public goods provision as part of the investment, can do so with the support of these instruments. This provides benefits to society that avoid higher public expenditure.

A similar argument can be employed for coordination and collaboration between external action funds and the EU Trust Funds, where enhanced coordination can lead to much stronger impacts and influence than a range of multiple, unaligned grant aid programmes and development lending with higher risks and costs due to a lack of joint collaboration.

Other savings are presented in a study commissioned by the European Parliament, which estimates the savings achieved by seven EU agencies avoiding the duplication of administrative bodies. The report concludes that the savings are considerable for both treasuries and the agencies’ clients. There are two reasons for this: the first is that the multiplication of agencies is unlikely to create the same costs as a single entity; but more importantly, with a centralised system which caters for all clients, they only need to approach a unique body, with single procedures, rather than several. This implies there is also a cost reduction for the clients. In exchange, the agencies recover most of the budget through service fees. In 2015, these agencies disposed of a budget of €1 025 million, of which €947 000 (92 %) was covered by fees. The European Union Intellectual Property Office (EUIPO)
is even totally self-funded. The authors of the report do not believe that such cost recovery through fees would be possible through multiple agencies. Furthermore, an approach based on ‘atomised’ agencies would make harmonisation of procedures very difficult and create barriers to the free movement of goods and services, increasing costs for all involved.

Other areas of savings

According to the above-mentioned ECORYS study, the highest impact in terms of returns on investment is gained through expenditure that enhances competitiveness, e.g. research and innovation, cross-border energy, transport and ICT structures, support for businesses, etc. The EU funding in these areas, and the EFSI support provided, are more likely to have a larger impact on GDP than investment in infrastructure and social funding for poorer regions. These benefits also increase revenues for the state.

The ECORYS study also mentions that high returns at EU level are to be gained from climate action and cross-border environmental issues. With the new EU green deal, and in particular the focus on energy transition, the EU budget aims at reinforcing EU influence in tackling global objectives. Only a coordinated EU effort in these fields can expect to have any impact at global level. The impact of separate national policies and bilateral deals would be unlikely to create the same return per euro spent, nor influence decisions taken abroad.

Many studies have analysed the impact of the EU budget, and, with the exception of the sometimes controversial subject of the common agricultural policy, other expenditures generally show positive results. Opinion is divided on cohesion policy, however. While, according to some studies, impact has been positive for net recipients and for the EU overall, due to the spillover effects, other studies have questioned this positive conclusion. The OECD for example, acknowledges the amelioration of the policy, but highlights the needs for various further improvements. Nevertheless, the OECD also highlights the benefits of EU programmes enhancing administrative capacity and governance.

Beyond direct transfers of EU funding, the EU budget has deep implications for national strategic planning, as well as financial and budgetary control. Recipients of support are expected to align to EU standards of planning, expenditure and monitoring. While there are still considerable problems in some Member States, EU standards are already embedded in national procedures, from procurement to monitoring. Without the financial support, backed by rules, a number of Member States would likely lag far behind.

Since 2000, the European Commission has introduced a large number of reforms to its financial management and control and while the EU budget still suffers from its past reputation, the quality of programmes in terms of strategy and financial control have considerably improved. The benefits of the push for performance and efficiency are being reaped by those countries that have taken the challenge seriously. Growth performance in Member States with solid strategies and clear expenditure priorities are growing faster. EU funds can help to spur the strategic quality of national investments.

Generally, however, for large impacts, notable efficiency increases and savings, the EU budget is far smaller than it should be. According to the theory of fiscal federalism an efficient distribution of competences between the national and EU level would require a larger budget. In fact, with the need for a stabilisation mechanism for the Eurozone few economists would recommend a smaller EU budget. Limiting EU expenditure to today’s level therefore reduces rather than increases savings and returns to the European economy and to individual Member States.

What can be done to save more and create greater value?

Academic research on the role of the EU budget generally claims that a larger, well targeted, EU budget can create better returns for the EU and its Member States. Action at EU level, including for
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Economic stabilisation (even if this may be carried out through the European Stability Mechanism (ESM) and not via the budget), can improve overall welfare in the EU, with benefits spilling over to net contributors beyond their share of transfers alone. In other words, the EU budget can achieve more than separate Member State action, or achieve the same with less funding (therefore creating savings).

If improving the impact of the EU budget and maximising overall savings is the objective, funding would need to increase in several key areas of common interest, with the appropriate mechanisms in place for ensuring performance.

However, the EU faces a serious barrier to expanding its operations, i.e. the lack of trust between Member States. Member States need to make an effort to improve in a few areas, where they should better align the following:

- Public accounting standards to improve trust between Member States. National accounts are often not complete, lack transparency and do not fulfil International Public Sector Accounting Standards (IPSAS). The introduction of advance public financial management tools would also enhance effectiveness and increase trust among not only Member States, but also taxpayers. The EU budget itself follows IPSAS in full today.

- National budgets to well-grounded strategies and integrate EU support in the most cost-effective way to achieve their goals. The EU budget should provide added impulse to key priorities rather than crowding-out investments or reducing national expenditure. Beneficiary regions should not design programmes for absorbing funds, but to create well-designed programmes that can be supported by EU funds.

The EU budget was designed to assist in bringing Member States together and to compensate them for the potential negative impacts of integration. Today, we are seeing the need for deeper integration and a budget that helps solve serious common goals. For such a budget, more and better targeted funding would bring more returns on investment and savings but would also require greater pooling of resources. It can also be concluded that:

- If the EU budget did not exist, Member States would have to provide many services and costs that it covers by themselves. Member State treasuries would have higher costs to achieve the same objectives and citizens would have to bear these costs. Without the EU budget, the EU single market would not function, creating costs for citizens and creating an overall economic impact.
- For net contributors, avoided payments to the EU budget are unlikely to make up for the lost economic returns to the treasury from additional tax returns created by stronger economic activity in the single market and from benefits of enhanced common action.
- Many opportunities and benefits are taken for granted by citizens (and governments), but are in fact an integral part of the functioning of the EU and its institutions, financed by the EU budget.
- For the EU to achieve its objectives cost effectively the Member States should pool more resources, not less.

As final ‘food for thought’, is providing savings the main raison d’être of the EU budget? The budget must also be seen in the context of the political reality of the Union. The cost of EU membership is, in gross terms, approximately 1% of EU GDP, and the highest net contribution to date was 0.4% of GNI in 2018 (from the Netherlands). The EU budget is the instrument to address common challenges and supports the continued existence of the EU through financial solidarity. The EU is a peace project, holds up the deepest common rules based free trade agreement in the world (the single market) and has introduced the revolutionary concept of EU citizenship, i.e. seeking full equality of rights and opportunities for all EU citizens regardless of their national origin. Is membership of such
a revolutionary Union of countries not worth the contribution of 0.4 % of GNI (approximately 1 % of public expenditure)?
ENDNOTES


2 ECORYS (2008), A Study on EU Spending, Commissioned by the European Commission, Directorate General for Budget, Final Report

3 The contribution to the EU Budget to cover the cost of the CAP can be estimated by isolating the costs and distributing it as share of the GNI resource. This allows to estimate the actual share of self-financing.


5 Ibid (2016)


7 For a review see Blomeyer, Roland & Paulo, Sebastian & Perreau, Elsa. (2017). The budgetary tools for financing the EU external policy, study for the European Parliament BUDG Committee.


9 European Union Intellectual Property Office (EUIPO), European Aviation Safety Agency (EASA), European Medicines Agency (EMA), European Chemicals Agency (ECHA), European Banking Authority (EBA), European Securities and Markets Authority (ESMA) and the European Insurance & Occupational Pensions Authority (EIOPA).

10 The Commission staff working paper accompanying the impact assessment of the Horizon 2020 proposals (SEC(2011) 1427 final) of 30 November 2011, presents estimations that each Euro spent in the EU 6th and 7th Framework Programmes has increased the Value Added in the business sector by €13.

11 For example see Malan J. (2016), ‘The ‘Cost of Non-Agencies’ with Relevance to the Internal Market’, analytical study for the Directorate General for Internal Policies, Policy Department D: Budgetary Affairs.


14 The OCED ranks the EU budget at the highest level compared in performance budgeting to other OECD countries. OECD (2017), ‘Budgeting and Performance in the European Union - A review in the context of EU Budget Focused on Results’, ECD Journal on Budgeting Volume 2017/1.


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