The European Union Budget Revenues after Brexit

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DOI: 10.36250/00749.48

JEL Classification: K34, F020

Abstract
This paper discusses legal and financial aspects of Brexit with a main focus on conditions needed for efficient generation of the revenues of the European Union. The paper is not definitive as Brexit negotiations are not complete yet; it aims to provide an update of legal changes that shape the ability of the European Union to maintain the revenue side of the Multiannual financial framework 2014–2020. The primary purpose of this contribution is to confirm or disprove the hypothesis that in effect of Brexit the European Union will lose the revenues and that new reforms concerning new revenues are necessary. To achieve the abovementioned goal, it will be necessary to describe the issue of the revenues of the European Union and then estimate the amount that will lack in the EU's budget after Brexit.

Keywords
Brexit; revenues of the European Budget; customs union; common commercial policy

1 Introduction

By invoking Art. 50 of the Treaty on the functioning of the European Union (consolidated version from 2012, C326/01) on 29 March 2017, the UK Government has started a process of Brexit negotiations that has both legal and financial consequences on the EU budget revenues. Both the scope of changes and their magnitude can influence

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Reiwer-Kaliszewska, A. The European Union Budget Revenues after Brexit. In: Hulkó, G. and Vybíral, R. eds., *European Financial Law in Times of Crisis of the European Union*. Budapest: Dialóg Campus. 2019. pp. 505–514.
DOI: https://doi.org/10.36250/00749.48

the EU's ability to fulfil legal obligations regarding ongoing and future budgetary expenditures in the multiannual perspective.

The primary purpose of this contribution is to confirm or disprove the hypothesis that in effect of Brexit the European Union will lose the revenues and that new reforms concerning new revenues are necessary. It seeks to do so by first describing the issue of the revenues of the European Union and then by estimating the amount that will lack in the EU's budget after Brexit. As the exit negotiations are not finalized yet in full, thus conclusions in this article are preliminary in their nature.

The method statement includes a literature review with respect to the impact of Brexit negotiations concerning legal changes and implications on revenue composition in financial terms. Sources of information include official documents of the EU and UK regarding the budgets of the EU and the UK respectively, plus recent joint negotiation reports of the parties concerned.

2 The Revenues of the Budget of the European Union

The issues concerning the budget of the European Union have been regulated in the Treaty on the Functioning of the European Union. According to Art. 311 of the TFUE, the European Union shall provide itself with the means necessary to attain its objectives and carry through its policies. Without prejudice to other revenues, the budget shall be financed wholly from own resources.

Revenues collected by the European Union are composed of Member States' contributions based on payments in proportion of each country's gross national income (GNI), collection of value added tax (VAT), traditional own resources (TOR) and other incidental revenues (like donations) and corrections. This article is focused on the total EU own revenues, as the nature of Brexit would impact all EU revenue line items in multiple time periods.

Current rules regarding the own resources of the European Union have been established by the Council Decision 2014/335/EU, Euratom. This Decision has been effective since 1 October 2016 after the ratification by all Member States according to their constitutional rules. The retroactive effects of the Decision 2014/335 applied from 1 January 2014 have been accounted for under the amending budget number 5/2016 adopted on 1 December 2016. The structure of the total amount of own resources by the type of own resource and by Member State is determined pursuant to the application of the rules laid down in the Council Decision on own resources and its implementing regulations. According to the Decision the total amount of own resources is capped at 1.20 % of the gross national income (GNI) of the EU. General view of EU own revenue sources is presented in Figure 1.

Table 1. Consolidated annual accounts of the European Union in EUR millions, presenting contributions from all 28 Member States EU own revenues 2009–2016

EUR m	2009	2010	2011	2012	2013	2014	2015	2016
GNI based contribution	81,978	91,178	88,442	98,061	110,194	104,688	95,355	95,578
VAT based contribution	12,795	12,517	14,763	14,871	14,019	17,462	18,328	15,859
TOR	14,002	16,065	16,528	16,087	15,467	17,137	18,649	20,439
Subtotal	108,775	119,760	119,733	129,019	139,680	139,287	132,332	131,876
Other revenue	1,762	2,568	4,944	1,900	8,579	11,338	10,554	14,311
Total revenue	110,537	122,328	124,677	130,919	148,259	150,625	142,886	146,187

Source: European Commission, 2017a

Excluding the impact of "other revenues" presented in Table 1, the total revenues amounted to EUR 131,876m for the year 2016. The report on budgetary and financial management regarding the year 2016 presents a higher number of EU revenues amounting to EUR 133,677.[2] Out of this amount, the UK has contributed EUR 17,979m (European Commission, 2017b), which is 13% of the total revenues for the year 2016. UK contribution is nonetheless the third largest after Germany (EUR 25,405m) and France (EUR 22,232m) and thus the lack of such revenue source may be hard to replace. Based on revenue data from the year 2009 to 2016 the revenues of the budget of the European Union are ranging from the level of EUR 126bn to EUR 143bn (the mean value is EUR 135bn). Thus, the contribution of the United Kingdom should be assessed, as well in order to assess the future revenue reduction impact. UK contribution from the year 2009 to 2016 ranged from EUR 10,111m as minimum in the year 2009 to EUR 21,409m as maximum in the year 2015.

As the revenues of the budget of the European Union in the period 2009 to 2016 were not the same and UK contributions also varied, we can estimate that the European Union is likely to lose from EUR 13.4bn to EUR 17.5bn revenues following Brexit. The most likely share of the UK in the total revenues is EUR 15.5bn divided by EUR 135bn, which is 11.5%. Yet this amount is underestimated, as for the purpose of calculation, legal revenue titles like surplus external aid guarantee fund, other incidental revenues, as well as surplus from previous year should be excluded (European Commission 2017a). Based on regular, recurring income contribution from Member States, the total revenues of the budget of the European Union in the years 2009 to 2016 were lower, which increases UK share to 12.2% on average (see Table 2).

2 This amount is based on the 6th amendments of the EU budget for the year 2016. Difference results from different grouping of "other revenues" and timing of EU reports.

The latest budget for the year 2017 has been amended six times during that year and each time UK contribution has been recalculated (Amending Budget No. 6 of the European Union for the financial year 2017, OJ L 21 of 25/01/2018). This makes it more difficult to track the current level of individual Member States' contributions.[3] Based on the latest 6th revision of the EU budget 2017, the contribution of the United Kingdom amounts to a high level of 16% (see Table 3).

Table 2. UK contribution to the EU budget in the year 2009 to 2016

Revenues in EUR m	2009	2010	2011	2012	2013	2014	2015	2016
UK contribution excl. rebate	10,112	14,659	13,825	16,178	17,110	14,072	21,409	17,979
Total TOR recurring	108,907	119,075	119,995	129,430	139,744	132,961	137,335	132,166
UK share	**9%**	**12%**	**12%**	**12%**	**12%**	**11%**	**16%**	**14%**

Source: European Commission, 2017b

Table 3. The contribution of the United Kingdom in 2017 to the EU total budget revenues

2017 EU budget after rev. No. 6 in EUR m	UK	EU total recurring revenues
Customs and sugar levies	3,134	20,374
VAT	3,316	16,620
GNI based resources	12,047	78,356
UK rebate	– 4,932	0
Reduction of GNI contribution to certain Member States	169	0
Total	**18,666**	**115,350**

Source: EU Monitor, 2018

3 EU Revenues during Brexit Negotiations

As the UK is a major contributor to EU revenues, a direct consequence of Brexit would be a permanent decrease of EU budget revenues. This would put more pressure on Germany as No. 1 remaining contributor of the Union, which is perhaps politically unacceptable (Kafsack, 2016). In 2016 the German Parliament has requested an

3 As of writing this article, the Consolidated annual accounts for the year 2017 have not yet been published.

economic report that shows the negative impact of Brexit on Germany as a result of potential new customs and trade barriers, which reduce German export, endanger jobs related to this market and ability of the country to contribute financially (Koenig, 2016). Therefore, during the Brexit negotiation round in December 2017, the European Union and the UK has prepared a joint report that is an initial basis for all legal, civil, trade and financial relations after Brexit (Joint report from the negotiators of the European Union and the United Kingdom government on progress during phase 1 of negotiations under article 50 TEU on the United Kingdom's orderly withdrawal from the European Union) (EU, UK, 2017).

The core legal principle is an "all or nothing" agreement, which increases stakes of both parties to reach a mutually acceptable final agreement. A part of this report is focused on the financial settlement with the EU and thus has a direct impact on future EU budgets and the forecasted revenue level. The first component of the proposed settlement is that the United Kingdom shall contribute in full for the years 2019 and 2020 as if it has not left the European Union. Consequently, the United Kingdom shall enjoy the famous rebate as if nothing happened and reduce financial liabilities further in case any surplus exercise happened until 2020 inclusive. As part of the financial commitments incurred during this period, yet payable in the subsequent years, the amount is defined as Reste à liquider (RAL).[4] The main financial question is how to define and recognise the UK's liabilities resulting from different legal sources. A part of the negotiated results is that the United Kingdom shall not participate in sharing of liabilities after 2020, which do have their own assets, i.e. Union financial assistance loan assets. Second part is a cut-off date 31 December 2020 regarding contingent liabilities and related to legal cases, i.e. resulting from financial guarantees underwritten by the European Investment Bank (EIB), together with a sweetener provision that any financial recoveries shall be shared as well by the parties. The United Kingdom shall receive from a future EU budgets funds regarding the share of net assets of the European Coal and Steel Community in liquidation, as well as the European Investment Fund as of 31 December 2020. However, it has been agreed that the United Kingdom shall not recover any funds regarding joint programs like EGNOS, Galileo and Copernicus and only after a discussion about future usage of these satellite-based services by the UK shall be decided.

During negotiations concluded in December 2017 report legal principles for financial separation have been established. The first principle is regarding the currency of financial settlement. It has been agreed that EUR shall be that currency, which reduces any financial risk for the remaining Member States, yet increases the long-term currency risk on the UK public finances. The third is that the United Kingdom shall not finance any new commitments not requiring funding from the Member States. The European Court of Auditors shall verify the level of commitments, decommitments and any assigned revenues that will become the RAL. The United Kingdom shall contribute

4 This clause can enable British institutions that participate in multiannual EU programs to finalise them without the need of abrupt reduction of funding.

pro-rate to the EU budget for the years 2019 and 2020, yet not more than the ratio of the own resources made available by the United Kingdom from the year 2014 to 2020 and the own resources made available by all Member States, including the UK. It has been agreed that timing of any UK payments until the end of 2020 shall be as bills fall due, not at any up-front arbitrary date. As some EU institutions personnel, like the European Union, European Defence Agency, the European Union Institute for Security Studies and the European Union Satellite Centre have offered pension as well as other post-employment benefits, the United Kingdom has to cover their share of these high value long term liabilities. The cut-off date has been agreed on 31 December 2020, yet payments shall be spread throughout the years, as any earlier one-off payment of these liabilities is highly sensitive to the real interest rate applied in the Net Present Value calculations. The UK Government estimates of financial settlement payments to the EU budget in the calendar based fiscal years have been presented in Table 4.

Table 4. EU financial settlement components and assumed payment periods in EUR bn

	Payment period	Amount	
		€ billion	**£ billion**
Total	**2019–2064**	41.4.	37.1
of which			
UK participation in EU annual budgets to 2020	2019–2020	18.5	16.4
Reste à liquider	2021–2028	20.2	18.2
Other net liabilities	2019–2064	2.7	2.5

Source: Chote et al., 2018

Timing of these payments is not equal and shall reduce sharply after the initial years (Figure 1). The amounts are lower than figures shown for the EU above, as they include UK's both public and private sector receipts from the EU as offsetting transactions.

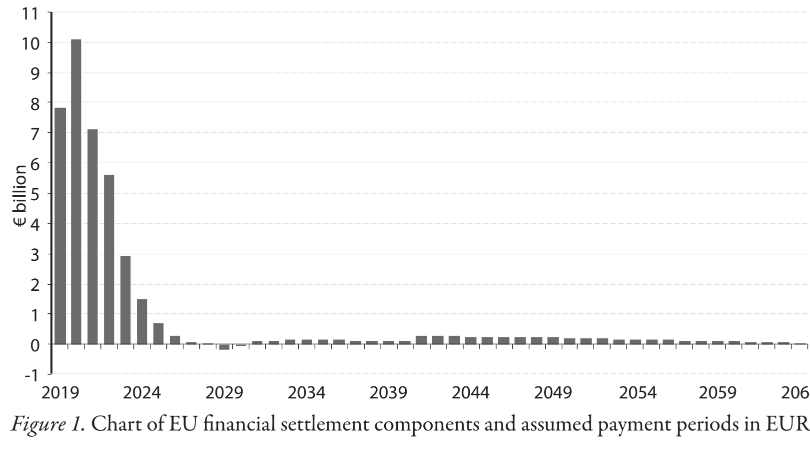

Figure 1. Chart of EU financial settlement components and assumed payment periods in EUR bn

Source: Chote et al., 2018

Exact amount of UK payments is not just pro-rata distributed among years, as the European Commission has the right to request up to five months' worth of total GNI and VAT contributions lest the UK rebates in the first quarter of the year, to take account of frontloaded Common Agricultural Policy (CAP) payments (Chote et al., 2018). In case the UK remained a full Member State, the Office for Budget Responsibility has provided initial figures until the year 2023 (Table 5).

Table 5. Total UK contributions to the EU if the UK remained an EU member

	€ billion							
	Outturn	Estimate	Forecast					
	2016	2017	2018	2019	2020	2021	2022	2023
GNI based contribution (a)	17.5	12.6	14.9	17.7	17.9	17.5	17.1	16.9
VAT payments to the EU (b)	3.6	3.3	3.4	3.4	3.4	3.5	3.6	3.7
Traditional own resources (c)	3.8	4.0	3.9	3.8	3.8	3.8	3.8	3.8
Notional contribution (d)=(a+b+c)	**24.9**	**19.8**	**22.1**	**24.9**	**25.1**	**24.8**	**24.5**	**24.3**
TOR collection costs (e)	–0.4	–0.8	–0.8	–0.8	–0.8	–0.8	–0.8	–0.8
UK abatement (f)	–6.7	–5.1	–4.8	–4.7	–5.4	–5.3	–5.2	–5.2
Gross contribution (g)=(d+e+f)	17.8	13.8	16.5	19.4	19.0	18.8	18.5	18.4
Public sector receipts from the EU (h)	–4.3	–5.6	–5.6	–6.3	–6.6	–6.6	–6.6	–6.7
Public sector net contribution (i)=(g+h)	**13.5**	**8.3**	**10.9**	**13.0**	**12.4**	**12.2**	**11.9**	**11.7**
Private sector receipts from the EU (j)	–2.8	–2.8	–1.7	–2.0	–2.0	–2.0	–2.0	–2.0
UK total net contribution (k)=(i+j)	**10.7**	**6.5**	**9.2**	**11.1**	**10.4**	**10.1**	**9.8**	**9.7**

Source: Chote et al., 2018

Based on data from Table 5 it can be seen that the gross UK contribution to the EU budget (without any receipts by the UK's public nor private sectors) varies between EUR 13.8bn for the year 2017 to 19.4bn in the year 2019, which is in the higher-level area compared to the initial simulation from Table 3, which ignores GNI growth as a factor increasing the amount of the contribution. This validates the hypothesis that UK's contributions to the EU budget is substantial and very soon the lack of these funds shall be visible both on the revenue and expenses side of EU budgets.

4 EU Budget Adjustments Proposed for the Multiannual Financial Perspective

On 2 May 2018, the European Commission adopted a draft European Union multiannual budget for 2021–2027 in the amount of EUR 1.28 bn. In the draft budget, the European Commission proposed to make the payment of EU funds dependent on compliance with the rule of law. An application regarding the suspension or limitation of funds for a given country will be submitted by the European Commission and accepted by the Member States. The budget for cohesion policy is to be reduced by approximately 7%, and for the Common Agricultural Policy by approximately 5%.

This draft has faced a lot of criticism from some of the largest EU's contributors. France protested against the 5% reduction of the Common Agricultural Policy program. The European Commission's new seven-year budget is also unacceptable for the Netherlands, as it represents a large increase in the Netherlands' EU bill. Due to Danish Prime Minister Lars Løkke Rasmussen, a "smaller EU should mean a smaller budget". He added that the European Union "cannot ask European taxpayers to pay for Brexit".

5 The Reform of the System of Own Resources of the European Union

In June 2017, the Commission adopted a Reflection Paper on the Future of the EU Finances [COM(2017) 358]. In this paper it proposed a range of options where the Own Resource should be linked more visibly to the policies of the European Union, particularly the Single Market and sustainable growth. Introducing the new Own Resources, special attention should be paid to their transparency, simplicity and stability, their consistency with the policy objectives of the European Union, their impact on competitiveness and sustainable growth and their equitable breakdown among Member States. The European Parliament adopted a Resolution on the reform of the system of the Own Resources in March 2018, highlighting the shortcomings in the present way of financing the budget and calling for discontinuation of all corrections and introduction of different new categories of Own Resources.

On 2 May 2018, the European Commission issued a proposal for a Council Decision on the system of Own Resources of the European Union [Com(2018) 325 final]. The Commission stated that the United Kingdom's withdrawal from the European Union, as well as the array of the new political priorities that have budgetary consequences call for particular attention to the architecture of the Own Resources system.

The Commission proposed to modernise the existing Own Resources system by maintaining the customs duties as Traditional Own Resources for the EU unchanged. However, the percentage the Member States retain as "collection costs" will decrease from 20% to 10%. The Own Resource based on Gross National Income are going to be kept as the balancing resource. Another aim is to simplify the Value Added Tax based on Own Resource.

The Commission also proposed to introduce a basket of new Own Resources. It would consist of a 3% call rate of the relaunched Common Consolidated Corporate Tax Base, to be phased in once the necessary legislation has been adopted, which should bring about EUR 12bn per year. Also, a 20% share of the auctioning revenue of the European Emissions Trading System, which depending on the actual carbon price, could bring EUR 3bn. Another source contemplated by the Commission is a national contribution calculated on the amount of non-recycled plastic packaging waste. The rationale for this tax is both environment protection (as oceans are flooded with plastic waste) as an incentive and also as a new source of EU own resources, which at price of EUR 0.8 per kg should bring EUR 7bn on an annual basis (European Commission, 2018).

Other goals of the Commission are to establish the principle that future revenues arising directly from EU policies should flow to the EU budget, discontinuing correction mechanisms and increase the Own Resources ceiling.

6 Conclusions

Although Brexit has been a surprise for many, this event can have a positive impact on a fundamental restructuring of EU budget own revenue sources. EU needs a solid and stable revenue streams to support multiannual framework expenditures. Thus, although the loss of UK related revenue stream is going to be painful for countries who are net EU payers through higher contributions, or recipient countries with lower EU funding level after the year 2020, it is also an opportunity to simplify the calculation of individual countries' contributions and diversification of revenue streams, which increase the stability and predictability of the EU own revenue resources. Thus, the hypothesis of an overall lower EU budget revenues level after Brexit has been confirmed. Also, the hypothesis that deep structural and spending quality building reforms regarding the EU budget expenditure side are needed after Brexit related revenue reduction is confirmed. Future co-operation with the UK should be based on fulfilling the amount of RAL, gradual payment of long-term liabilities and per usage-based payments for EU funded services that the UK continues to use, like the Galileo project and its military grade quality GPS location precision that the UK helped to create. By stronger linking of EU policies with revenue sources, including a higher level of protection of natural environment, the new legal framework proposed in May 2018 by the Commission may have a positive impact not only on the level of EU finances, but also on the air we breathe in.

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