ARTICLES

CENTRAL EUROPEAN REVIEW OF ECONOMICS & FINANCE
Vol. 43. No 2 (2023) pp. 37-51
DOI https://doi.org/10.24136/ceref.2023.008

Katarzyna Stabryła-Chudzio[1]

BUDGETARY OPERATING BALANCES IN THE ASSESSMENT OF THE FINANCIAL ASPECTS OF EUROPEAN INTEGRATION

Abstract:

The aim of the study was to assess whether the presentation of financial flows between states and the EU budget provides constructive information, since the literature on the subject emphasizes that the assessment of the benefits and costs of integration has a much broader and more complex scope resulting from the free movement of people, services, goods and capital.

In the paper it was used data from 2019 taking into consideration the last year of the UK's full membership in the European Union and a year before COVID-19 pandemic which also has influenced EU finance. In addition, the current operating balances of the member states are presented based on the latest data from 2022 referring to the author's modified algorithm for calculating operating budgetary balances according to the guidelines of the European Commission.

Findings resulting from the conducted research are as follows: referring to the formulated hypotheses it should be stated that there are no grounds to reject them. Correction mechanisms on the revenue side of the European Union budget affect the operating balance of a given country, although they do not have to cause a change in the operating balance from negative to positive or vice versa. In addition operating budgetary balances do not provide a true picture of the benefits and costs of European integration.

[1] *PhD, Cracow University of Economics, College of Economics, Finance and Law, Institute of Finance, Department of Finance and Financial Policy, 27 Rakowicka Street, 31-510 Cracow, Poland,* e-mail: stabrylk@uek.krakow.pl

Providing the value of budget balances for member states in relation to the EU budget should be considered a strictly accounting procedure. The wider use of operating budgetary balances can be considered a denial of the essence of European added value, because they refer to the idea of "fair return" as the expectation of a certain adequacy between the amounts paid and the funds received from the budget.

Keywords: operating budgetary balances, European Union budget, correction mechanism. financial solidarity.

JEL codes: F15, H30, H77.

Introduction

The results of analyzes concerning payments and withdrawals to and from the European Union budget has been controversial since the beginning of the European Communities. As new areas were covered by joint expenditure and new members were admitted, the problem of budget balances increased, and the division into net payers and beneficiaries led to many misunderstandings between member states and an often misleading interpretation of this accounting concept.

The aim of the article is to assess whether the presentation of financial flows between states and the EU budget provides constructive information, since the literature on the subject emphasizes that the assessment of the benefits and costs of integration has a much broader and more complex scope resulting from the free movement of people, services, goods and capital. The following hypotheses were adopted for the study:

1) Correction mechanisms on the revenue side of the European Union budget affect the operating balance of a given country.
2) Operating budget balances do not provide a true picture of the benefits and costs of European integration.

To examine the impact of transfers from and to the European Union budget in individual member states, data from 2019 was used due to the last year of the UK's full membership in the EU and a year before COVID-19 pandemic which also has influenced EU finance. In addition, the current operating balances of the member states are presented based on the latest data from 2022 according to the proprietary adjusted budget operating balances method used by the European Commission,

The study was divided into four main parts. The first one presented the essence of the division of EU countries into net contributors and net recipients and the importance for the perception of the benefits and costs of European integration. The second part was devoted to the evolution of the correction mechanisms existing on the revenue side of the EU budget.

The third part presents the methodology for calculating budget operating balances and research results, while the fourth part contains discussion and conclusions. The research used the European Commission's database dedicated to the revenues and expenditure of the EU budget.

1. The essence of budget operating balances

When publishing data on operational budget balances, the European Commission emphasized that they were of a strictly financial nature and therefore no conclusions could be drawn on their basis about the benefits and costs of membership in the European Union. However, despite the clear position of the European Commission, data on operating balances are used by member states for or against further deepening of integration. Such different views on financial flows often result from the conscious use of this data for specific, particular purposes of political parties. As a result, currently, i.e. referring to the multiannual financial framework for 2021-2027, the European Commission has stopped providing information on budget balances, although this data can be obtained based on payments and withdrawals in relation to the EU budget.

The budget balance calculated according to the European Commission's methodology is called the operational budget balance and is calculated according to the formula (European Commission, 2019):

$$OBB_i = TAE_i - AE_i - ANC_i \times \frac{TAE_{UE} - AE_{EU}}{ANC_{EU}} \qquad (1)$$

where:
OBB_i *operating budgetary balance* of the state *i*, where i = 27 or 28[2];

TAE_i *total allocated expenditure from the EU budget* for the state *i*, where i = 27 or 28, or i = EU for EU as the whole organisation;

AE_i *administrative expenditure*) for the state *i*, where i = 27 or 28, or i = EU for EU as the whole organisation;

ANC_i *adjusted national contribution* of the state *i*, where i = 27 or 28, or i = EU for EU as the whole organization.

The assumptions adopted by the European Commission do not include:

- on the side of expenditure from the EU budget, funds for EU administration, as expenditure for the common functioning of the European Union, and not for the benefit of a specific member state, and expenditure for third countries (those remaining outside the European Union, including candidate countries) are not taken into account; as a result, other expenses are called operational,

[2] Number of member states before or after British withdrawal from the European Union.

- on the side of revenues to the EU budget - traditional own revenues, currently in the form of customs duties, as a levy resulting from the functioning of the customs union, and therefore resulting from the import of goods into the European Union.

The European Commission's methodology for calculating budget operating balances is based on the assumption that it is a zero-sum game for the entire European Union (Asatryan et al., 2020a) i.e. how much a given member country could receive from the EU budget, taking into account the same percentage share as in payments to the EU budget. The value calculated in this way is then subtracted from the actual expenditure from the EU budget for the given country (Stabryła-Chudzio, 2022).

The presentation of budgetary operating balances is treated with great caution in drawing conclusions about the benefits and costs of integration on this basis alone. The net benefits go beyond operating balances and include wider economic and social impacts in terms of trade opportunities, employment and productivity, including spillover effects on other members. Furthermore, data on operating balances are only indicative from an economic point of view.

Therefore, a broader aspect of integration should be taken into account, relying on the following arguments (Asatryan et al., 2020b; Asatryan et al., 2020c):

- the existence of economies of scale of spending at EU level compared to spending at member state level,
- threshold effects of projects that, from a financial point of view, a single country would not be able to implement,
- cross-border effects, including: in the form of foreign direct investments, trade, environmental protection, scientific research results,
- effects of freedoms guaranteed by the European single market (movement of people, goods, services and capital),
- the existence of external expenditure from the EU budget not included in budget balances and intended for economic and social cooperation of third countries with the European Union, supporting democracy, protecting human rights and stability in a given region,
- the existence of other funds outside the EU budget that are not taken into account when calculating operating balances.

2. The importance of financial correction mechanisms in the European Union budget

The correction mechanisms existing in the European Union budget are considered to be a denial of the essence of European added value, because they refer to the idea of "juste retour", i.e. "fair return" as the expectation of a certain adequacy between the amounts paid and the funds received from the EU budget. The fear of excessive "crediting" to other members has prompted some countries to negotiate a number of correction mechanisms allowing them to reduce the amount of revenue they transfer to the EU budget (Stabryła-Chudzio, 2022).

Financial correction mechanisms include special discounts (rebates, reductions, abatements) relating to the amount of the contribution to the European Union budget (table 1). These rebates are on the revenue side of the EU budget, although they contribute to reducing the contribution rate. From a historical point of view, an attempt to introduce the first correction mechanism appeared in the 1970s, with the beginning of Great Britain's functioning in the European Communities. Subsequent discounts were introduced successively along with requests from selected net payers to reduce payments to the community budget. So far, Great Britain, Germany, Austria, the Netherlands, Sweden and Denmark have benefited from the discounts, but the amount of the discounts and their mechanism have changed over time.

Table 1. Corrective mechanisms in the history of the European Communities and the European Union

Before 2000
United Kingdom – British rebate (abatement, reduction) Germany – the so-called rebate on the British rebate, i.e. a 33% reduced payment to Great Britain
2000-2006
United Kingdom– British rebate Austria, Germany, Sweden, the Netherlands - the so-called rebate on the British rebate, i.e. a 75% reduced payment to Great Britain
2007-2013
United Kingdom – British rebate Austria, Germany, Sweden, the Netherlands - the so-called rebate on the British rebate, i.e. a 75% reduced payment to Great Britain Austria - reduced VAT rate (0.225%) Germany - reduced VAT rate (0.15%) Netherlands and Sweden - reduced VAT rate (010%); A flat-rate reduction in your GNI-based contribution
2014-2020
United Kingdom – British rebate Austria, Germany, Sweden, the Netherlands - the so-called rebate on the British rebate, i.e. a 75% reduced payment to Great Britain Austria – three-year flat-rate reduction in GNI-based contributions Denmark - flat-rate reduction of the GNI-based contribution Germany - reduced VAT rate (015%) Netherlands and Sweden - reduced VAT rate (015%); a flat-rate reduction in your GNI-based contribution
2021-2027
Austria, Denmark, Germany, the Netherlands and Sweden - flat-rate reduction in GNI-based contributions

Source: Asatryan et al. (2020a); Benedetto (2017, pp. 615-633).

It should be noted that the rebates apply to countries that pay more than they receive from the EU budget and therefore constitute a form of financial relief for the largest net contributors. As a result, correction mechanisms are associated with the concept of the so-called national budget balance, i.e. the relationship between the funds received from the EU budget by a given country and the contribution it pays.

From 2021, one official form of discount from the previously existing ones has been left, i.e. lump-sum corrections on the basis of the annual GNI-based contribution of Denmark, the Netherlands, Austria, Sweden, and Germany (table 2). The gross reductions is financed by all other member states, according to their GNI. Every year amounts are indexed based on the GDP deflator.

Table 2. Rebates per year in Multiannual Financial Framework 2021-2022 (m EUR)

Denmark	377
Germany	3 671
The Netherlands	1 921
Austria	565
Sweden	1 069

Source: https://commission.europa.eu/strategy-and-policy/eu-budget/long-term-eu-budget/2021-2027/revenue/rebates_en (retrieved June 18, 2023).

As Darvas (2019a) rightly notes it is also possible to distinguish a "hidden rebate" related to retaining a certain part of customs revenues as "collection costs", which benefits countries with an external EU border. A partially hidden rebate can also be called flat-rate payment limitations in some member states due to the collection of non-recyclable plastic packaging waste. However, there is a justification here in order to avoid excessive regressive impact on the contributions of member states whose GNI per capita in 2017 was lower than the EU average. In accordance with the EU Council Decision on the system of own resources of the European Union (Council of the European Union, 2020) this reduction corresponds to the value of 3.8 kilograms of non-recyclable plastic packaging waste multiplied by the population of the member state concerned in 2017[3].

3. Methodology and research results

This article uses the author's proposal to calculate operating balances in the context of actual payments and funds from the EU budget to member states, taking into account the European Commission's arguments regarding the omission of EU administration expenses and traditional own revenues

[3] The uniform call rate is EUR 0.80 per kilogram.

from the calculations. Consequently, the formula for the modified budget balance will be:

$$MOBB_i = (TAE_i - AE_i) - (TNC_i - TOR_i) \qquad (2)$$

where:
$MOBB_i$ – modified operating budgetary balance of member state *i*, where i = 27 or 28[4];
TAE_i - total allocated expenditure of member state *i*, where i = 27 or 28;
AE_i - administrative expenditures allocated to member state *i*, where i = 27 or 28;
TNC_i - total national contribution of member state *i* , with i = 27 or 28.
TOR_i – traditional own resources of member state *i* , with i = 27 or 28.

By total national contribution is understood:
- for multiannual financial framework 2014-2020 revenue based on GNI, value added tax and traditional own resources,
- for multiannual financial framework 2021-2027 revenue based on GNI, value added tax, revenue form non-recycled plastic packaging waste and traditional own resources.

In addition to the above-mentioned arguments questioning the reliability of operational budget balances, it should also be noted that data on operational budgetary balances for a given member state vary over time and also present a different picture when presented in relative values (e.g. in relation to GDP or per capita) and absolute (figure 1).

[4] Number of member states before or after British withdrawal from the European Union.

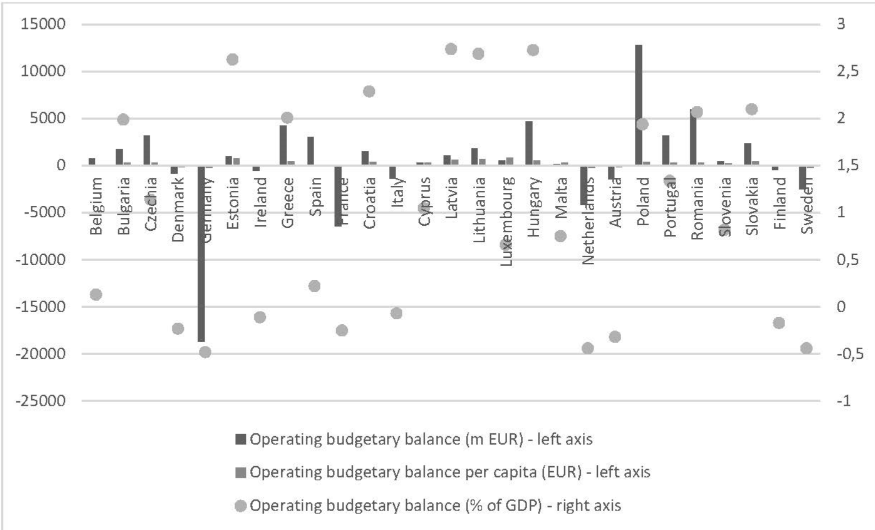

Figure 1. The amount of the modified operating budgetary balance in the EU member states in 2022

Source: own study based on European Commission data (retrieved July 1, 2023 from: https://commission.europa.eu/strategy-and-policy/eu-budget/long-term-eu-budget/2021-2027/spending-and-revenue_en).

From the chart above, it can be seen that in 2022, where Germany, France and the Netherlands were the largest net payers in EUR million, while in relation to GDP and per capita - Germany, Sweden and the Netherlands. In 2022, Poland, Romania and Hungary were the largest net beneficiaries in absolute terms, while in relation to GDP they were Latvia, Hungary and Lithuania, and per capita - Luxembourg, Estonia and Lithuania.

In 2022, net beneficiaries received EUR 50.4 billion more than they paid in, representing 0.32% of EU GDP. The increase in this amount compared to the average of the years 2014-2020 may result from the limitation of correction mechanisms. The number of net beneficiaries remained the same as in 2019 (18 countries), with Ireland becoming a net payer in 2022 and Belgium becoming a net recipient.

These differences confirm the difficulty in drawing clear conclusions about the balance of payments and withdrawals from the EU budget. However, it should be emphasized that 2022 was an exceptional year because it was the penultimate year of using funds from the 2014-2020 period, which was associated with increased expenditure from the EU budget, and at the same time, not all countries started spending funds from the new multiannual financial framework for 2021-2027. Moreover, for the 2021-2027 financial framework, a new source of financing was introduced in the form of revenue based on non-recycled plastic packaging waste.

Apart from Ireland, which became a net payer in 2022 compared to 2019 in absolute terms, Germany, France, the Netherlands, Austria, Finland and Sweden also recorded a deterioration in negative balances (figure 2). A deterioration of the positive balance was observed for Bulgaria, the Czech Republic, Croatia, Latvia, Hungary, Malta and Slovenia, while the positive balance of Luxembourg increased by over 1,228% and Belgium became a net beneficiary in 2022. The introduction of rebates improves the balance situation in 2022 in absolute terms for the beneficiaries of these mechanisms, i.e. Germany, Austria, Denmark, the Netherlands and Sweden.

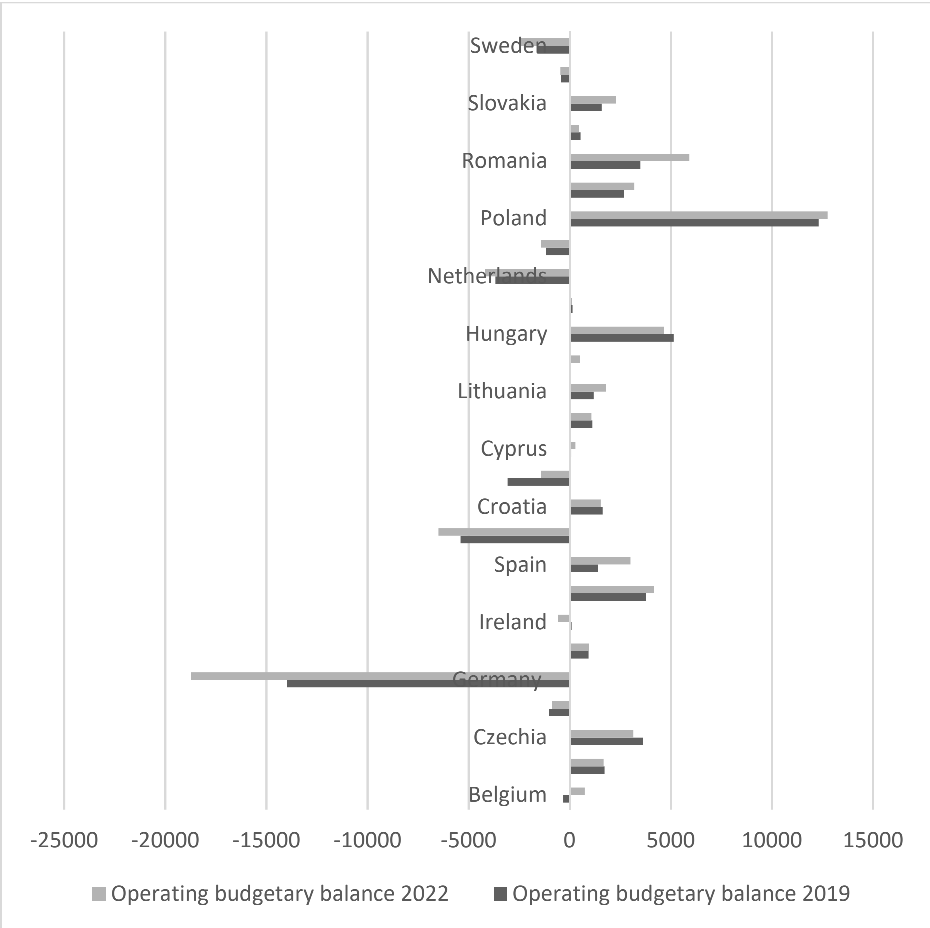

Figure 2. The amount of modified operating budgetary balances in 2019 and 2022

Source: own study based on European Commission data (retrieved July 1, 2023 from: https://commission.europa.eu/strategy-and-policy/eu-budget/long-term-eu-budget/2021-2027/spending-and-revenue_en).

Comparing the balances with the recognition of rebates in 2022 (figure 3), the balance of Bulgaria, the Czech Republic, Germany, Ireland, France, Croatia, Latvia, Hungary, Malta, Slovenia, Finland and Sweden deteriorated compared to 2019. The reasons could be threefold: firstly, the emergence of a new source of revenue from unrecycled plastic, or secondly, larger payments to rebate beneficiaries, or finally, thirdly, the deterioration of the budget balance itself.

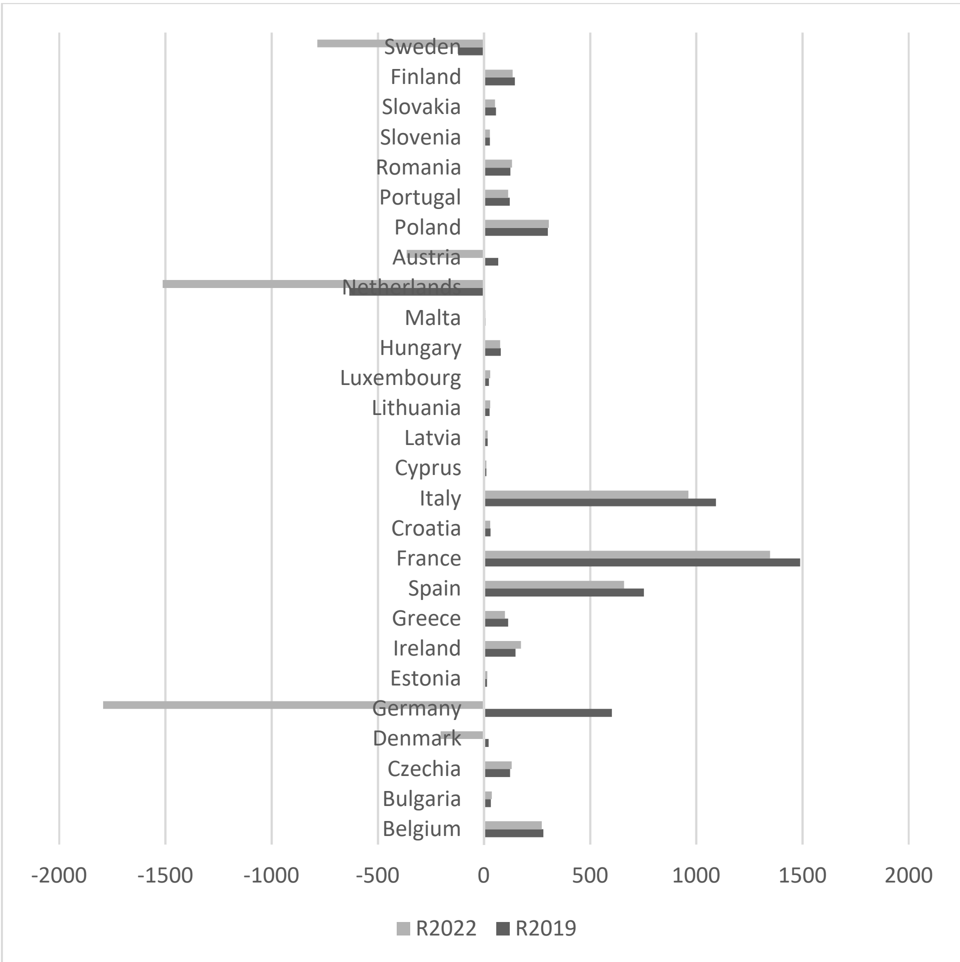

Figure 3. The amount of the correction mechanisms (R) in 2019 and 2022
Source: own study based on European Commission data (retrieved July 1, 2023 from: https://commission.europa.eu/strategy-and-policy/eu-budget/long-term-eu-budget/2021-2027/spending-and-revenue_en).

Therefore, a year-to-year comparison of operating balances will not provide the basis for drawing far-reaching conclusions, since the level of expenditure from the EU budget is significantly influenced by the level of advancement of investments co-financed from EU funds.

Darvas emphasizes (2019a, 2019b), that the desire of some countries to reduce their contributions to the EU budget is not due to the low level of wealth of the country in relation to the EU average, but from the desire to improve the net balance.

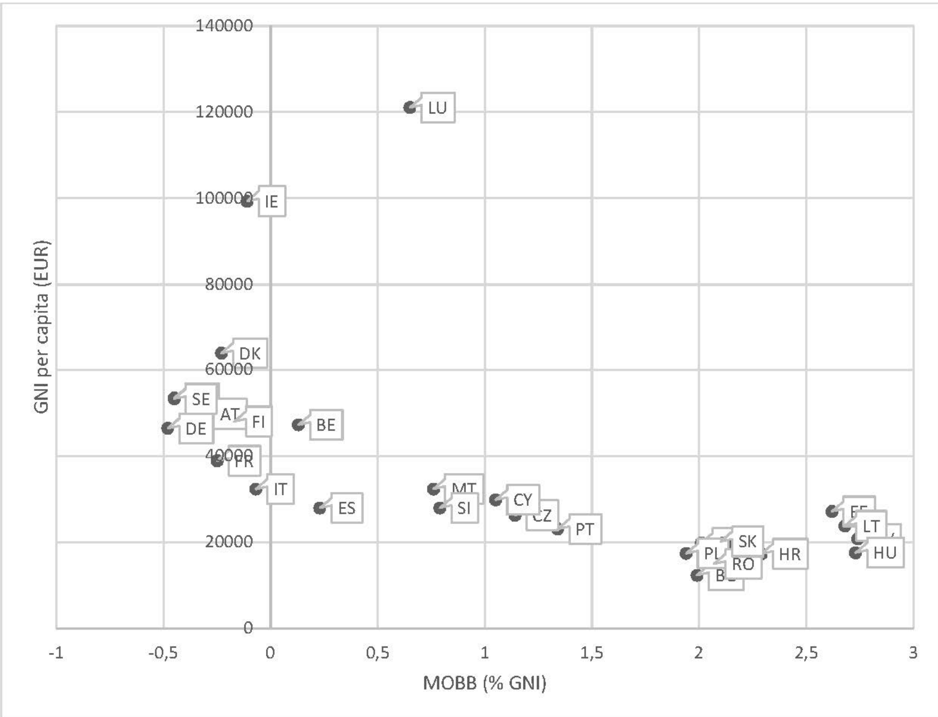

Figure 4. GNI per capita and modified operating budgetary balances in 2022
Source: own study, comp. Darvas (2019a, pp. 6-7).

Based on the conducted considerations, it can be concluded that there is an inverse relationship between the amount of modified operating balances and the wealth of countries, i.e. as the gross national income of a given country increases, its modified operating balance decreases. However, the relationship is not linear (figure 4), because the chart shows some exceptions, including: Luxembourg and Ireland as the wealthiest countries and at the same time not recording the lowest operating balances, and on the other hand Hungary, Latvia, Lithuania and Estonia with the highest positive balances in 2022 and at the same time not being among the least wealthy. Therefore, the effect of redistribution of funds from the EU budget is still dominant, although it relates mainly to cohesion policy and, to a large extent, to the common agricultural policy. The remaining directions of spending do not refer to national divisions, but to achieving functions of public finances other than redistribution, i.e. allocation and stabilization, also in the context of sustainable development.

4. Discussion

It can be noted that the role of budget balances in discussions on changing the structure of the EU budget is still alive, which results from great difficulties in measuring European added value. European added value, which translates into many areas, is also the core of considerations on the importance of the EU budget. However, problems in assessing the effectiveness of EU programs, both in terms of finding appropriate measurement tools and in the time needed to learn the final results of their implementation, cause EAV to become an opaque and complicated concept, and thus give rise to further use of the idea of "juste retour" (Schout & van Riel, 2023).

As Schout, Molthof and Hollander (2023) point out, leaving EU budget main revenue based on gross national income is the best solution in the current situation because it takes into account primarily the level of wealth of the member states in the contribution to the EU budget. Moreover, the calculation mechanism is understandable and transparent, although it requires adjustments after the final determination of the GNI amount for a given year. Nevertheless, it would also be necessary to abandon the correction mechanisms that complicate the relatively simple assumptions of GNI-based own resources.

It should be noted, however, that the gradual introduction of new sources of the European Union's own revenues without a direct national reference may in the distant future reduce the interest of member states in calculating net balances, but such a change in attitude would also have to be the result of a change in attitude regarding the shape of the European Union. For now, it seems impossible for the pro-federal direction to gain wider recognition among politicians and thus change the attitude from the national interest to the EU interest.

Moreover, the attempt to move away from the net balance approach solely by introducing new tax-based own resources of the EU budget is, for now, too small steps to draw far-reaching conclusions (Benedetto, Heinemann & Zuleeg, 2020). Additionally, the more expenditure categories will serve to achieve objectives at the EU level, and therefore the more expenditure will be related to achieving European added value, the less important the reference to the budget balance will be.

The debate on the importance of operational balances leads to the conclusion that as long as a significant part of the EU budget expenditure is based on the redistributive function, i.e. on the common agricultural policy and cohesion policy, member states will pay attention to the amount of the described balance. Only the transfer of the burden of spending to European public goods and the actual introduction of taxes of supranational importance can change the approach of member states.

To summarize this study, operating balances resulting from political bargaining can lead to distorted spending decisions (Santos & Neheider, 2009). Monti et al. (2016) are also negative about the perception of the EU budget as a zero-sum game. Oettinger and Crețu (2017) are in favor of abolishing all rebates, especially if this would result in real added value.

Conclusions

On the basis of the author's modified budget operating balance and the author's calculations of correction mechanisms, the significance of financial flows between the European Union budget and the member states was assessed. Referring to the hypotheses formulated at the beginning of the article, it should be stated that there are no grounds to reject them. Correction mechanisms on the revenue side of the European Union budget affect the operating balance of a given country, although they do not have to cause a change in the operating balance from negative to positive or vice versa.

Operating balances are considered to have a certain 'political appeal' (Heinemann, Pilati & Zuleeg, 2020) used for the needs of current national policy, thus shifting to the background European Union activities that are not the result of a top-down negotiated national division (so-called national envelopes). As a result, as the history of European integration shows, negotiations on changes in the structure of the EU budget are extremely complicated long and rarely lead to spectacular solutions (Stabryła-Chudzio, 2022).

Operating budgetary balances do not provide a true picture of the benefits and costs of European integration. Determining the benefits and costs of integration based on data relating to budget operating balances can be misleading and lead to incorrect conclusions. This tool is used in a purely accounting aspect and therefore cannot be treated as an assessment of the role played by the European Union budget (Asatryan et al., 2020c; Sapała, 2020). Therefore, it is necessary to consider the advisability of presenting operating balances.

Part of the answer can be found in an attempt to explain the existence of correction mechanisms in the EU budget. Net payers to the EU budget through revenue reductions are trying to look for ways to reduce their contributions, which means that the EU's revenue system has become complex and often incomprehensible to the public (Darvas, 2019a). It can, of course, be noted that after United Kingdom left the European Union, the rebate system was simplified somewhat automatically, i.e. the correction mechanism for Great Britain and the so-called rebate on the rebate, i.e. special discounts in payments towards the British rebate for selected countries while increasing the payments of other EU members. Moreover, it may also be a contribution to examining the evolution of the structure of revenue and expenditure of the EU budget, although not the only one and insufficient.

References

1. Asatryan, Z., Havlik, A., Heinemann, F., Nover, J., Pilati, M. (2020a). The net operating balances: Variants, emerging numbers and history. Brussels: Policy Department for Budgetary Affairs, Directorate-General for Internal Policies.
2. Asatryan, Z., Havlik, A., Heinemann, F., Nover, J. (2020b). Why net operating balances are a distorted indicator of a Member State's benefit from the EU budget. Brussels: Policy Department for Budgetary Affairs, Directorate-General for Internal Policies, European Parliament.
3. Asatryan, Z., Havlik, A., Heinemann, F., Nover, J., Pilati M. (2020c)., The net operating balances or the "Juste retour" approach. Brussels: Policy Department for Budgetary Affairs, Directorate-General for Internal Policies, European Parliament.
4. Benedetto, G. (2017). Institutions and the route to reform of the European Union's budget revenue, 1970–2017. Empirica, 44, pp. 615-633.
5. Benedetto, G., Heinemann, F. & Zuleeg, F. (2020). Strategies to overcome the '*juste retour*' perspective on the EU budget, Brussels: Policy Department for Budgetary Affairs, Directorate-General for Internal Policies.
6. Council Decision (EU, Euratom) 2020/2053 of 14 December 2020 on the system of own resources of the European Union and repealing Decision 2014/335/EU, Euratom (OJ L 424, 15.12.2020, pp. 1-10).
7. Darvas, Z. (2019a). A new look at net balances in the European Union's next Multiannual financial Framework Bruegel Working Paper, 10.
8. Darvas, Z. (2019b). Who pays for the EU budget rebates and why? Bruegel Blog, retrieved July 23, 2023 from: https://bruegel.org/2019/12/who-pays-for-the-eu-budget-rebates-and-why/
9. European Commission (2019), EU Budget 2018. Financial Report. Luxembourg: Publications Office of the European Union.

10. Heinemann, F., Pilati, M., Zuleeg, F. (2020). How to overcome the "juste retour"obsession. Brussels: Policy Department for Budgetary Affairs, Directorate-General for Internal Policies, European Parliament.
11. https://commission.europa.eu/strategy-and-policy/eu-budget/long-term-eu-budget/2021-2027/spending-and-revenue_en
12. https://commission.europa.eu/strategy-and-policy/eu-budget/long-term-eu-budget/2021-2027/revenue/rebates_en\
13. Monti M., Dăianu D., Fuest C., Georgieva K., Kalfin I., Lamassoure A., Moscovici P., Šimonytė I., Timmermans F. & Verhofstadt G. (2016). Future financing of the EU: final report and recommendations of the High Level Group on Own Resources. Luxembourg: Publications Office of the European Union.
14. Oettinger, G. H. & Crețu, C. (2017). Reflection paper on the future of European Union finances. European Commission, COM (2017) 358, Brussels.
15. Santos I. & Neheider S. (2009). Reframing the EU budget decision-making process. Bruegel Working Paper, 3.
16. Sapała M. (2020). Strengths and Weaknesses of the EU Budget Flexibility 'toolbox'. in B. L,affan and A. De Feo (Eds.), EU financing for Next Decade. Beyond the MFF 2021–2027 and the Next Generation EU (pp. 253-266). Florence: European University Institute.
17. Schout, A., & van Riel A. (2023). The State of Economic in the Eurozone, The Hague: Netherlands Institute of International Relations 'Clingendael.
18. Schout, A., Molthof, L. & Hollander, S. (2023). The Multiannual Financial Framework. The search for flexibility and recognised effectiveness. The Hague: Clingendael Report, Netherlands Institute of International Relations 'Clingendael'.
19. Stabryła-Chudzio, K. (2022). Kształtowanie europejskiej wartości dodanej w kontekście ponadnarodowych dóbr publicznych, Warszawa: Polskie Wydawnictwo Ekonomiczne.