

BLOG POST 24.05.2017

Brexit will shake up the EU budget and that's a good thing

Jörg Haas

Wissenschaftler beim Jacques Delors Institut – Berlin



Brexit will reshape the EU's finances. It forces the EU to choose between spending less and increasing national contributions. Jörg Haas argues that this could lead to conflicts about burden-sharing, but it could also offer a window of opportunity for overhauling the EU budget, a goal that has proven elusive for many years. A pragmatic package deal could include slightly higher member state contributions in return for an overhaul of the EU's spending priorities.

1 How does Brexit reshape the EU's finances?

Firstly, there is the “Brexit bill”. The EU and the UK need to agree how the assets and liabilities of the EU should be split. This will likely require a one-off payment by the UK that has been extensively discussed in the press over the last months.

Secondly, the EU will face a structural funding gap. Since the UK is a net contributor to the budget, there will be a revenue shortfall of around €10 billion per year even if the EU no longer spends any money on programmes in the UK.

Finally, Brexit will simplify the EU revenue system. The infamous UK rebate on budget contributions will disappear. This also will spell the end of the “rebate on the rebate”, an exception that reduces payments for some large net contributors.

The latter two effects have received less attention than the Brexit bill, but could ultimately prove more important for the further development of the EU. While Brexit will have an immediate effect on the EU's finances, the most important implications concern the next budgetary planning period, starting in 2021.

2 How to fill the Brexit gap?

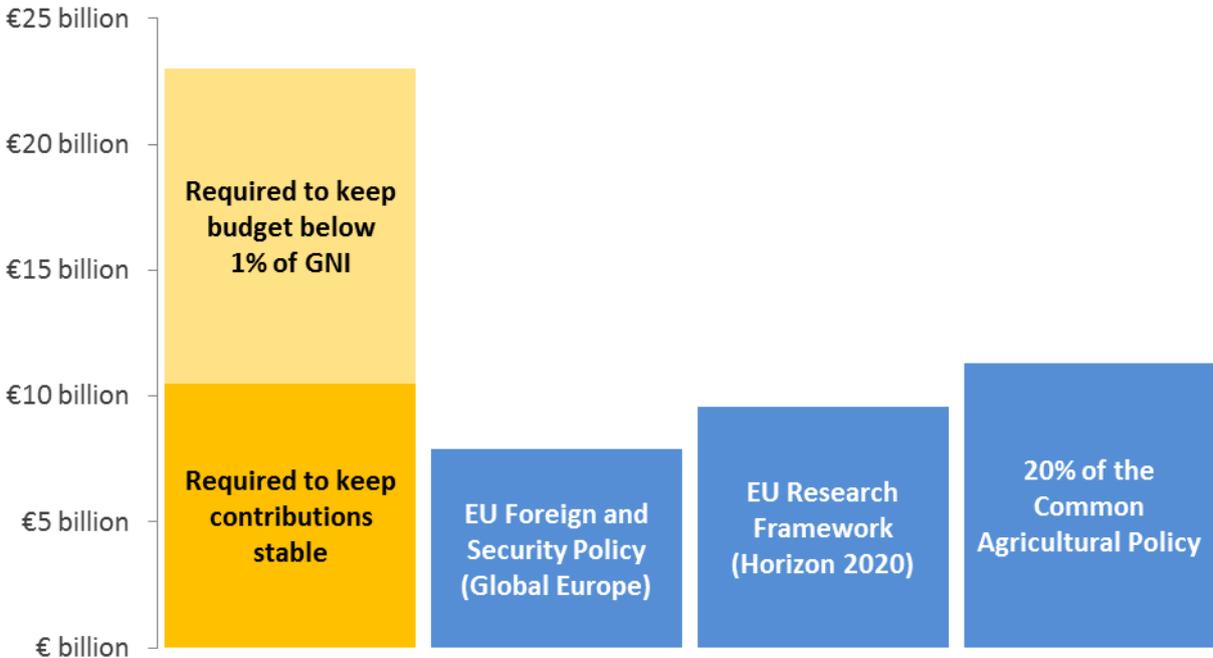
How can the EU address the €10 billion structural “Brexit gap” in its budget? Since the UK has ruled out large regular payments, Europe has to choose between increasing the contributions paid by the remaining member states (EU-27) and cutting the budget.

If national contributions to the EU budget are increased to make up for the shortfall, all countries will have to pay more according to their economic strength. In order to maintain the spending level of the EU-27, national contributions would need to increase by 8% on average. But more importantly from a political viewpoint, the increase would be highest for a number of countries that are already among the largest net contributors. This is because the aforementioned rebate on the rebate would disappear. Austria, Germany, The Netherlands and Sweden would consequently see their contributions increase by around 15%.

Cutting the budget might seem like an appealing alternative. An expenditure cut of €10 billion yearly would maintain national contributions constant. An even larger reduction of around €23

billion yearly would be needed to maintain spending at 1% of GNI, which has long been a political objective of the EU member states. But the impact of such a cut on the EU’s programmes should not be underestimated. In 2015, the entire European research framework, *Horizon 2020*, had a budget of €10 billion. All EU spending on foreign policy amounted to less than €8 billion. That reminds us that most EU spending still goes to cohesion policy (around €50 billion) and the common agricultural policy (almost €60 billion). Cutting either of them could balance the budget, but such a move would likely meet strong resistance from countries like Poland and Hungary.

Figure 1: Possible budget cuts compared to EU programmes (in 2015)



Source: Author’s representation, based on European Commission data.

3 What are the political implications?

It is easy to imagine two coalitions emerge in the negotiations about budget reform. The largest net recipients can be expected to defend today's budget, especially the programmes on cohesion and agriculture. Net contributors, especially those affected by the discontinuation of rebates, are likely to lobby for cuts or reforms. The two groups are not new, but Brexit drives them further apart.

There are no clear legal provisions for adjusting the EU budget to the departure of a member state. At the same time, unanimity is needed to change today's financial framework and to decide on a new one for the time after 2020. Therefore, a political compromise is unavoidable.

A positive outcome of the budget negotiations should not be taken for granted. Faced with net beneficiaries' desire to protect their receipts from cohesion and agricultural policy, and net contributors' desire to minimise the additional cost, the EU could get a budget that features the worst of both worlds: an old-fashioned budget centred on subsidies and a financing scheme that is complicated by a maze of rebates and exceptions.

Fortunately, there is potential for a good package deal. Countries such as Germany and the Netherlands could agree to contribution increases, but in return, the budget would need to be restructured. More money should be spent on areas where the EU can clearly create added value, such as research, migration, and the management of the common borders. Brexit opens a window of opportunity for ambitious budget reform. It is up to the EU member states to use it wisely.

This blog post was published on 23rd May 2017 on the website of [E!Sharp](#).