

# THE ANNUAL BUDGET AND MEDIUM-TERM FINANCIAL OUTLOOK OF THE EUROPEAN UNION

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*The operative financing of the European Community is based on the annual budget of the European Union. Given the number of countries in the European Union and other varied interests of these individual countries, the process of approving the budget can be a very complicated matter. Therefore budgeting in the European Union is based on respecting the principle of a medium-term financial outlook. This sets priorities in common activities that have been transferred to the European Union by means of primary legislation<sup>1</sup> and the maximum limits on the financing of these priorities. In 1999 the financial outlook for the years 2000 – 2006, was proposed, where a new feature of this outlook was the designation of expenditures for pre-accession aid to candidate countries. Through the agreement of the European Commission, the Council of the European Union and the European Parliament there was stipulated the principle that the maximum amount of expenditures of the European budget may not exceed 1.27% of the gross national product of the member states of the European Union, and indeed the European budget has never reached this level. Following the decision on the accession of a further 10 candidate countries as member states in December 2002 in Copenhagen, the financial outlook was adjusted, taking into account that the sums agreed in the framework of accession negotiations, where it is this financial outlook that now currently applies. The European Commission on 10 February 2004 published a financial and political outlook of the European Union for the years 2007 – 2013.*

*It is expected to be passed by the Council of the European Union and the European Parliament in mid-2005. The aim of the following contribution is to specify differences of national budgets and the European Union budget, to highlight the genesis of the development of its incomes and expenditures, to familiarise the reader with the stages of compiling the European Union's annual budget and to list the main priorities that the European Union is to finance over the period 2007 – 2013.*

## Differences between National Budgets and the Annual Budget of the European Union

National budgets of individual member states differ from the general budget of the European Union (hereinafter also referred to as “the EU budget”) primarily in the following ways:

1. Size – the state budgets of the member states in relation to the gross national product (GNP) normally range around a share of 40% or more. The size of the share of the EU budget in the gross national product of the European Union over the years 2000 - 2006 may not exceed the limit of 1.27%.

2. Balance – the state budgets of the member states are proposed as deficit budgets, the EU budget must always be balanced.

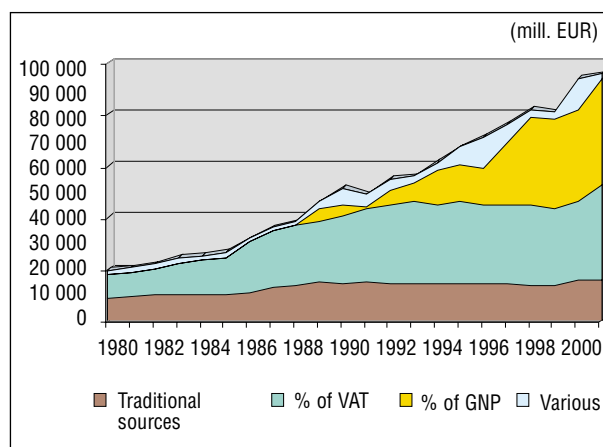
3. Orientation of expenditures – the main expenditures of national budgets are directed towards the social field, while those of the EU budget are directed primarily to the Common Agricultural Policy and Structural Operations.

4. Income sources – incomes of the state budgets of

member states are tax and non-tax, whereas the EU budget has set and limited sources of income:

- customs and customs fees – are imposed on imports from non-member countries on the basis of the Common Customs Tariff,

Graph 1 Development of incomes of the EU Budget



European Community (sometimes termed also the Treaty on European Union – 1992), which was amended by the Treaty of Amsterdam (1999) and the Treaty of Nice (2001). Primary legislation is also deemed to include the Single European Act (1986), Acts on the Accession of New Member States (1972, 1979, 1985, 1994, 2002) and the Merger Treaty (1965).

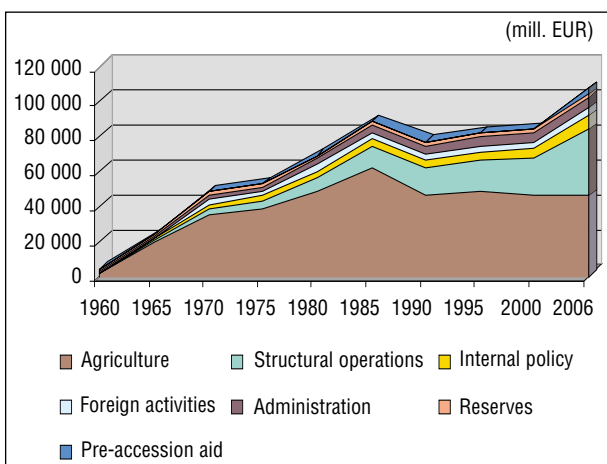
<sup>1</sup> By primary legislation we mean: The Treaty on the Founding of the Coal and Steel Community (1951), The Treaty Establishing the European Atomic Energy Community and the Treaty Establishing the European Economic Community (1957), this treaty was re-named in Maastricht to the Treaty Establishing the



- agricultural fees – are imposed on the import of agricultural products from non-member states,
- a share in income from value-added tax (VAT) in individual countries (approximately 1.4% of VAT)
- a share in the GNP of individual countries (according to the degree of economic prosperity, max. 1.2% of GNP).

The graph depicting the incomes of the EU budget over the past 20 years shows that the volume of traditional sources (customs and agricultural fees have remained at approximately the same level, their share in the total incomes in 2001 being slightly below 17%. Incomes from VAT have gradually grown and their share in 2001 was 38%. The most dynamic growth has been seen in the share of GNP of individual countries, reaching 43% and various sources<sup>2</sup> represented 2% of the total incomes of the EU budget.

**Graph 2 Development of expenditures of the annual budget and the medium-term financial outlook of the European Union**



The graph of the development of EU budget<sup>3</sup> expenditures shows that a substantial part of the expenditures is used for financing agriculture and without reforms in this field it is not possible to substantially reduce the general expenditures of the European Community. The second largest group of expenditures comprise structural operations.

### Principles Applied in Compiling the European Union Budget

The process of compiling the EU budget is founded on two principles:

1. The effort to achieve the most efficient use of resources, which is conditional upon reform of the Common Agricultural Policy and Structural Operations, as the two largest items of expenditure.

<sup>2</sup> Incomes designated as various include, for example, fines paid by individual countries for breaches of EU legislation, as well as budget surpluses from preceding years.

The Graph to 2002 contains current data. Data for the years 2003 – 2006 are from the medium-term financial outlook.

2. Solidarity between individual states, in particular from the aspect of fulfilling the budget.

### Stages in Compiling the Annual Budget of the European Union

The stages in the process of compiling the annual budget are sometimes termed “the budget life cycle”. The procedure of drafting and passing the budget is similar to that in individual countries. The whole budgeting process takes four calendar years.

Year: R-1	
January	European institutions prepare their own operating budgets for the following year Y
May	The European Commission on the basis of the documents from individual institutions presents a preliminary draft budget (PDF) for the year Y
July	The Council of the EU discusses and supplements the preliminary draft budget for Year Y
October	First reading of the budget in the European Parliament
November	Second Reading by the Council of the EU
December	Second reading of the budget in the European Parliament. The chairman of the European Parliament through signing confirms the budget for Year Y
Year: R	
January to December	The European Commission implements the annual budget
Year: R+1	
January to November	The Court of Auditors exercises financial control over the fulfilment of the annual budget
November	The Court of Auditors publishes its annual report
Year: R+2	
March	The Council of the EU checks the reports of the Court of Auditors and adopts recommendations for the European Parliament
Spring	The Committee on Budgetary Control of the European Parliament discusses the reports of the Court of Auditors and the Council of the EU and performs a concluding confirmation

Throughout 2003 the historic budget of 2004 for the enlarged European Union was under preparation. It was approved upon its second reading in the European Parliament on 18 December 2003. The total volume of expenditures was approved at the level of 0.98% of the Gross National Product of the European Union (EUR 99 724 billion). The whole cycle ends, as does the budget, only in 2008.

### Medium-Term Financial Outlook of the European Union

The main aim of the medium-term financial outlook is to maintain financial discipline, thus fixing the upper limit



of budgetary expenditures. Further aims are to ensure continuity in planning and lastly to improve cooperation between the institutions cooperating in the budgetary process of the European Union. Budgetary discipline was insufficient in the 1980's (as is clear from the graph on budgetary expenditures) and the annual formation of the budget was greatly hampered. The European Union institutions responsible for financing common activities<sup>4</sup> agreed on drawing up the first medium-term financial outlook in 1998 for the period of 5 years.

The medium-term financial outlooks to date have served for financing the Single European Act (1988 to 1992 the "Delors I Package"), the implementation of the Maastricht Treaty (1993 – 1999 "Delors II") and the enlargement of the European Union (2000 – 2006 "Agenda 2000"). The period of these outlooks has ranged from 5 (Delors I) to 7 (Delors II, Agenda 2000) years. At present the financial outlook applies until 2006.

### The Medium-Term Financial Outlook of the European Union and its Updating

In 1999 as a part of the negotiations concerning the Agenda 2000 a plan of the financial prospects was adopted for the period of seven years (2000 – 2006). This financial outlook limited the level of contributions for the enlargement of the European Union by states of Central and Eastern Europe without threatening the main priorities of the EU. The structural funds of the EU over the years 2000 – 2006 are one of the main instruments of solidarity between Europeans – in this way they assist in the creation of jobs, as well as the economic develop-

#### Medium-term financial outlook of the European Union 2000 – 2006 as prepared in 1999 (percentage shares)

	2000	2001	2002	2003	2004	2005	2006
Agriculture	44.50	45.82	46.28	46.36	45.82	45.34	45.44
Structural operations <sup>5</sup>	34.84	33.67	33.41	33.24	33.32	33.36	32.85
Internal policy	6.43	6.45	6.51	6.66	6.86	7.04	7.23
Foreign activities	4.93	4.87	4.84	4.87	4.94	5.00	5.05
Administration	4.94	4.91	4.98	5.11	5.28	5.43	5.59
Reserves	0.97	0.94	0.67	0.43	0.43	0.43	0.41
Pre-accession aid	3.38	3.33	3.31	3.32	3.36	3.39	3.42
Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00

<sup>4</sup> The general budget is decided upon by the Council of the European Union and the European Parliament. It is prepared and implemented by the European Commission.

<sup>5</sup> Structural operations are financed by means of the Structural Funds (European Regional Development Fund, European Social Fund, European Agricultural Guidance and Guarantee Fund, Financial Instrument for Fisheries Guidance) and the Cohesion Fund.

ment of less developed regions through investing in education and infrastructure.

#### Medium-term financial outlook of the European Union 2003 – 2006 prepared in 2003 (percentage shares)

	2003	2004	2005	2006
Agriculture	43.93	44.02	43.39	43.93
Structural operations	35.08	35.18	35.94	35.08
Internal policy	7.70	7.62	7.55	7.70
Foreign activities	4.51	4.43	4.37	4.51
Administration	5.31	5.36	5.41	5.31
Reserves	0.39	0.39	0.38	0.39
Pre-accession aid	3.07	3.01	2.96	3.07
Total	100.00	100.00	100.00	100.00
Max. payments as % of GNP	1.15	1.12	0.17	0.18
Max. payments according to Agenda 2000 as % of GNP	1.27	1.27	1.27	1.27

On 11 February 2003 the European Commission<sup>6</sup> adopted a proposal for an amendment to the financial outlook for the years 2004 – 2006 in order that the demands ensuing from enlargement agreed in December 2003 in Copenhagen are fulfilled. This proposal thus reflects the process of incorporating the 10 new member states in the framework of the limits agreed for the 6 candidate countries in Berlin in 1999.

The ceilings for agriculture and structural funds agriculture and structural funds, internal policy and administration were increased by the amount agreed at Copenhagen. Internal policy contains resources such as "Schengen" for better control of external borders, for atomic safety in Lithuania and in Slovakia, as well as for building up administrative and institutional structures.

The ceiling for pre-accession aid remained unchanged. The Commission is proposing a gradual increase in the amount of finance for Bulgaria and Romania. A support programme for Turkey will also be supported from this item in 2004. The volume of financial support will double by 2006. The Commission has drawn up a special scenario in the case that a political solution to the Cyprus question will be found.

<sup>6</sup> By the Member of the European Commissioner for Financial Issues Michael Schreyer (Germany)

## Medium-term financial outlook of the European Union for 2007 – 2013

On 10 February 2004 the European Commission presented a financial and political outlook for an enlarged Europe for the years 2007 – 2013 supporting the Union's priorities. In Romano Prodi's view the main priorities are: sustainable development, the interests of inhabitants of the European Union and a strengthening of the international position of the European Union<sup>7</sup>.

*Sustainable development:* growth, cohesion and employment. The Council of the European Union in 2000 in Lisbon set the goal of catching up with the USA and Japan by the end of the decade in research and scientific technologies. Therefore it is essential to strengthen science and research, increase the quality of education and training, and invest in the competitiveness of busi-

nesses in the framework of the internal market. Growth and competitiveness are the main priorities in the framework of regional policy, the basis of which is aid to less-developed areas of Europe. A common policy in the field of fishing will continue in the sustainable exploitation of resources.

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### Medium-term financial outlook of the European Union 2007 – 2013 (prepared in 2004 (percentage shares))

	2007	2008	2009	2010	2011	2012	2013
Sustainable development	39	45	45	46	47	47	48
Natural resources	46	43	42	41	40	39	37
of which agriculture	36	33	31	30	29	28	28
Internal policy	1	1	1	2	2	2	2
Foreign policy	9	9	9	9	9	10	10
Administration	3	3	3	3	3	3	3
Compensation	1	0	0	0	0	0	0
Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00
Max. payments as % of GNP	1.15	1.23	1.12	1.08	1.11	1.14	1.15
Max. planned incomes as % of GNP	1.24	1.24	1.24	1.24	1.24	1.24	1.24

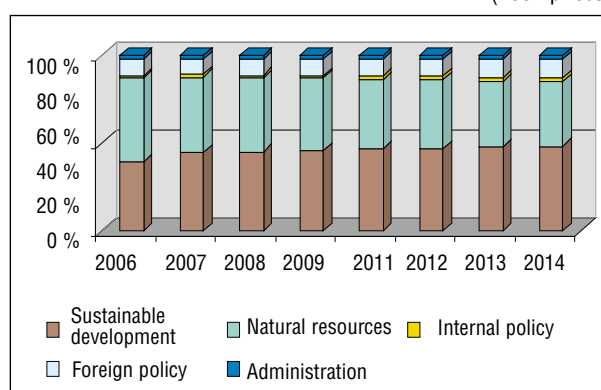
nesses in the framework of the internal market. Growth and competitiveness are the main priorities in the framework of regional policy, the basis of which is aid to less-developed areas of Europe. A common policy in the field of fishing will continue in the sustainable exploitation of resources.

The Commission proposed to implement realistic reform of the Common Agricultural Policy founded on the market valuation of agricultural products by 2013. Direct payments from the field of agriculture will be used in regional development programmes.

*Interests of inhabitants of the European Union.* In 1999 the Council of the European Union in Tampere outlined the main components of the European model of society: freedom, security and justice. Currently the issues of immigration, asylum policy, the fight against crime and terrorism, which cannot be solved adequately at the national

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Graph 3 Financial framework of the European Union 2007 – 2013 (2004 prices)



<sup>7</sup>[http://europa.eu.int/rapid/start/cgi/guesten.ksh?p\\_action.gettxt=gt&doc=IP/03/1769|0|RAPID&lg=EN&display=](http://europa.eu.int/rapid/start/cgi/guesten.ksh?p_action.gettxt=gt&doc=IP/03/1769|0|RAPID&lg=EN&display=)