Net Contributions to the EU Revisited

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Introduction

The EU budget negotiations have been dominated by the logic of ´juste retour´ which entails that member state´s contributions and receipts should be in a fair balance. This logic is clearly at odds with the principle of solidarity among member states, and ignores the concept of a European public good of which the value added by definition cannot be ascribed to one member state (like external security or mitigating climate change). In practice, the contributions and receipts of member states are not exactly offsetting. Since its foundation, the EU has lodged two types of member states: net contributors and net recipients. Yet, the concept of ´juste retour´ prevails during budget negotiations, always echoing Margaret Thatcher´s famous statement ´I want my money back´. As a rule, the net contributors want to cut on the current budget, whereas the net recipients want to preserve the current budget. With the U.K. as net contributor leaving and with higher ambitions in the field of security and migration, the negotiations on the post-2020 Multiannual Financial Framework (MFF) of the EU will be more difficult than ever.

The logic of 'juste retour' is in this paper accepted and extended. It brings together insights and estimates from other public sources to arrive a fresh perspective on the spoils in the European Union.

First, it applies also to the allocation of European agencies. After the Brexit referendum, the European Banking Authority and the European Medical Agency had to be relocated and were fought over. Especially, the fight for EMA was hard. Slovakia was furious that he EMA would not come to Bratislava that it did not participate in the voting anymore. That lead to a run-off between Amsterdam and Milan where the votes were a tie and the lot had to decide. But does the relocation of EBA to Paris and the EMA to Amsterdam really affect the balance of contributions and receipts across member states? Despite the furious fight, the answer is: not really.

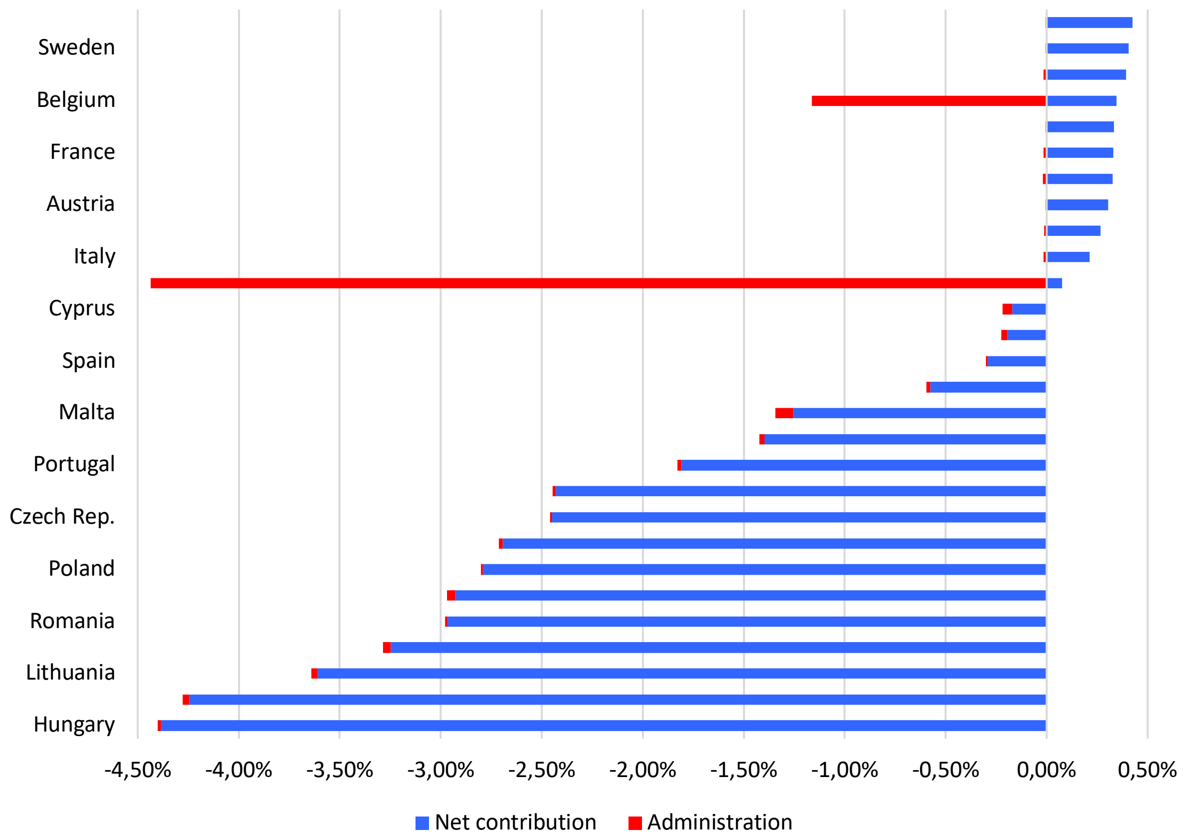
Second, the logic of 'juste retour' also applies to corporate taxes. The European member states fight, also among each other, for the corporate tax base and in that sense for the right to tax corporate profits. Recent estimates by Zucman et al. (2018) shed light on the gains and losses stemming from profit shifting within the EU, which enables us for the first time to account for profit shifting when calculating the net contributions of member states. It turns out that a majority of the member states is deprived of a substantial part of their corporate tax base by a minority of six EU tax havens. Although we draw upon official statistics and existing research, the results are new to our knowledge.

Redistribution through the EU Budget

We first look at the official statistics on the current net contributions of member states to the EU budget. The member states contribute each year to the EU budget, mainly by means of a percentage levied on their gross national income (GNI). This already implies that the rich contribute more than the poor do. At the same time, member states receive funding from the EU budget for a range of programs including agriculture, regional policy (cohesion and structural funds) and research & development. The difference between these contributions and receipts equates a member state´s net contribution. Figure 1 shows the average net contributions as a percentage of GNI over the period 2012-2016. All eastern European member states and most southern European member states have been net recipients, while most northwestern member states have been net contributors. In relative terms, the largest net contributors are Germany, Sweden, and the Netherlands and the largest net recipients are Hungary, Bulgaria, and Lithuania.

It clearly appears from Figure 1 that the relatively rich member states pay for the relatively poor member states. The differences in gross national income across the Union are still very significant. The implication is that the net contributions by Germany, Sweden and the likes are not more than 0.5% but the net receipts often exceed the 2%.

Figure 1. Average net contribution to EU budget by member state (% GNI), 2012-2016[1]



[1] Note: The net contributions are calculated as total national contribution (incl. UK correction and lump sum reduction granted for DK, NL, AT and SE) minus total EU receipts (excl. administration) by member state. *Source: European Commission (2017); http://ec.europa.eu/budget/figures/interactive/index_en.cfm, own projections*

Redistribution through European institutions and agencies

When accounting for the benefits of member states that are hosting some of the EU institutions and agencies, the result that rich pay for poor member states is distorted. Figure 1 shows in particular that the net contributions of the rich countries Belgium and Luxembourg changes completely. Belgium that hosts the Commission, the Parliament, and the Council turns from a net contributor into a net recipient. And Luxembourg that hosts the Court of Justice, the Court of Auditors, and the Investment Bank even becomes one of the largest net recipients. So, clearly, hosting an EU institution or agency can be a lucrative business as it could change ones *de facto* net contribution substantially. That is why many member states have bid to host the European Medical Agency (EMA) - which will relocate to Amsterdam - and the European Banking Authority (EBA) - which will relocate to Paris - that are leaving the United Kingdom over Brexit.

The United Kingdom has benefited from the location of the two agencies EBA and EMA within London. But it has benefited to a much lesser degree than Belgium and Luxemburg as Figure 1 already illustrates. Indeed, if one considers the expenses under the heading 'administration' in the EU budget, these are roughly 150 million euro in the years 2014 and 2015. This does not really affect the UK's net contribution that amounts to several billions in euro. This is also true of the net contributions of France and the Netherlands.

It is however the case that the expenses on the EU budget are a poor measure for the benefits. For example, just a small part of the EMA budget is financed from the budget; the main source comes from fees. Nevertheless, other studies do not overturn the idea that the agencies are a net benefit to France and the Netherlands but these benefits are small when compared to the net contributions by these two countries.

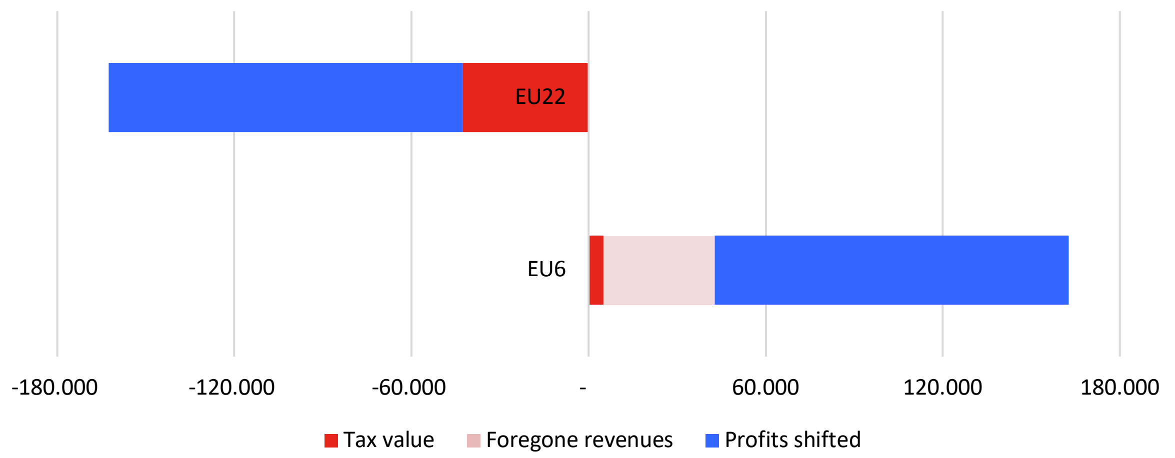
A recent study performed by ING Bank (2018) shows that the Netherlands could gain 250-300 million euro from the construction of the new headquarter and up to several tens of millions each year, stemming from the housing and daily expenses from the agency´s employees. This does yet not account for the impulse it could give to pharmaceutical related research institutes and businesses in the Netherlands.

Redistribution through profit shifting in the EU

The logic of 'juste retour' also applies to profit shifting. The member states compete to attract the corporate tax base, i.e. profits, and in the process redistribute corporate tax revenue. Recently, Zucman et al. (2018) estimated the amount of profits shifted towards tax havens, including six EU tax havens (Ireland, Netherlands, Luxembourg, Belgium, Malta and Cyprus) as a result to international tax competition. The results show that the amount of excess profits reported in these six tax havens (dubbed as the ´EU6´) is 293 billion euro, of which as many of 55 percent stems from the other EU countries (dubbed as the ´EU22´). Figure 2 shows that that each year 163 billion euro in profits is shifted out of the EU22 into the EU6.

One could very well say that profit shifting is a rather inefficient instrument for redistribution. First and foremost, a great deal of the tax revenue are lost in the process of redistribution. The loss in tax revenues for the EU22 is 42.8 billion euro whereas the gain in tax revenue for the EU is only 5.1 billion, according to Zucman and others. On the same tax base the EU6 levies on average a far lower rate than the EU22. Hence, the net loss of profit shifting comes down at an amount of 37.6 billion euro.

Figure 2. Profits shifted to EU tax havens (m EUR)



Source: Zucman et al. (2018), own projections

The foregone tax revenues of 37.6 billion euro are effectively excess profits that are not taxed, but that are retained in the business, mainly benefitting a small group of shareholders. Revenues that could have been used for public services like schools and hospitals or to boost jobs and growth, now end up in the pockets of today´s super-rich like Jeff Bezos and Mark Zuckerberg. Thus, the EU tax havens are not only depriving the other member states from a valuable tax base worth billions of euros in tax revenues, but are taking just a small part of the pie for themselves, leaving the rest to corporates. This fundamentally goes against the core idea of solidarity and partnership.

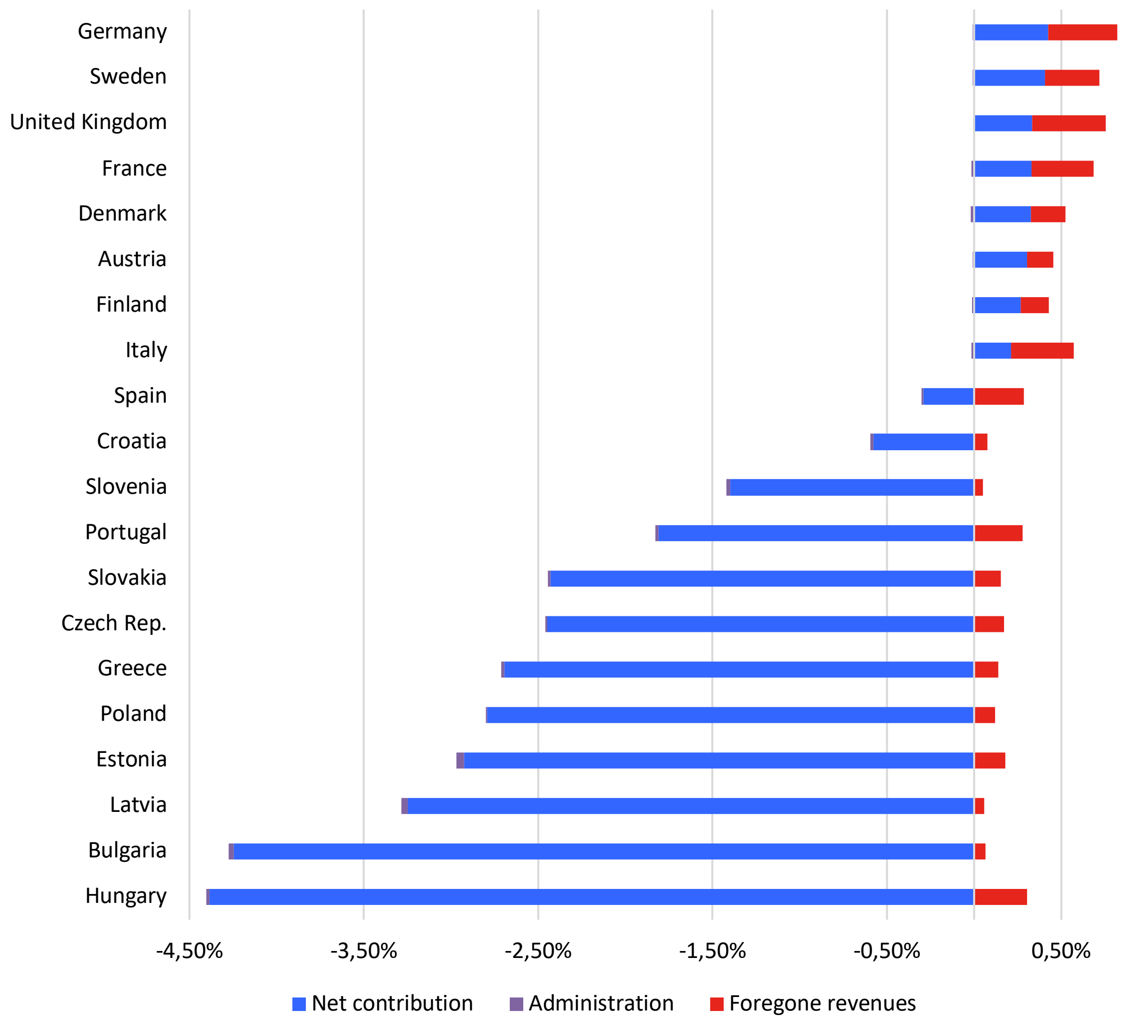
The Net Contributions Revisited

We argue that the official statistics misrepresent the *de facto* net contributions of the EU tax havens, because they do not capture the sums of profits they attract from other member states. Therefore, we revise the net contributions by accounting for the gains and losses from profit shifting within the EU, as estimated by Zucman et al. (2018), from three different perspectives.

- **Revised net contributions of the EU22**

  First, we add the foregone revenues of the individual EU22 member states to their net contributions. Figure 3 shows how this would change the *de facto* net contributions for these member states. It clearly illustrates that the losses from profit shifting (i.e. foregone revenues) are largely borne by the large member states with relatively high corporate tax rates. For instance, the relative net contributions of Germany and France become twice as high, while those for the United Kingdom and Italy even more than double. The foregone revenues of Spain are estimated to offset their net receipts. Also the northern member states Sweden, Denmark and Finland become much larger *de facto* net contributors when accounting for their losses.

Figure 3. Revised net contributions of the EU22 (% GNI)[2,3]



- ***What are the costs of the EU6 for the EU (European perspective)***

Second, we assign the foregone revenues for the EU22 to the individual EU tax havens according to their relative share in the total amount of profits attracted by these havens[4]. This allows us to compare the net contributions for the EU budget of the EU6 with the costs they impose on the other member states.

Figure 4 clearly shows that the costs for EU stand in stark contrast with the net contributions to the EU budget. For example, the Netherlands costs the EU 13.8 billion euro in foregone revenues, while they only contribute 2.6 billion euro to the EU budget. And the already net

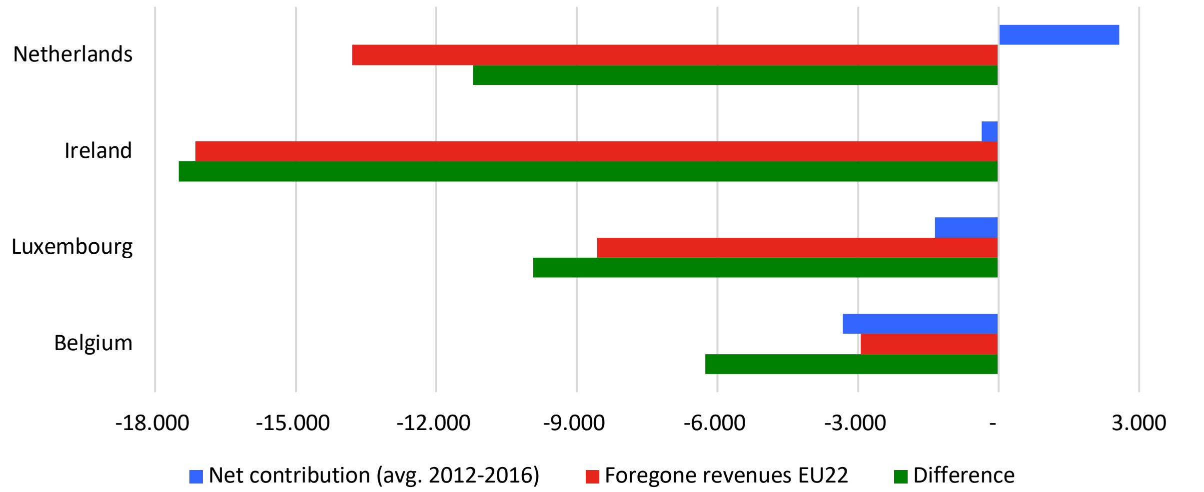
[2] See figure A of the appendix for the absolute foregone revenues of the EU22

[3] Note: The net contributions are calculated as total national contribution (incl. UK correction and lump sum reduction granted for DK, NL, AT and SE) minus total EU receipts (excl. administration) by member state. *Source: European Commission (2017); http://ec.europa.eu/budget/figures/interactive/index_en.cfm and Zucman et al. (2018), own projections*

[4] Ireland (40%), Netherlands (32%), Luxembourg (20%), Belgium (7%), Malta (1%)

recipients Ireland, Luxembourg, and Belgium are even a much larger cost to the EU when accounting for the losses due to profit shifting.

Figure 4. The costs of four EU tax havens for the EU (mio EUR)

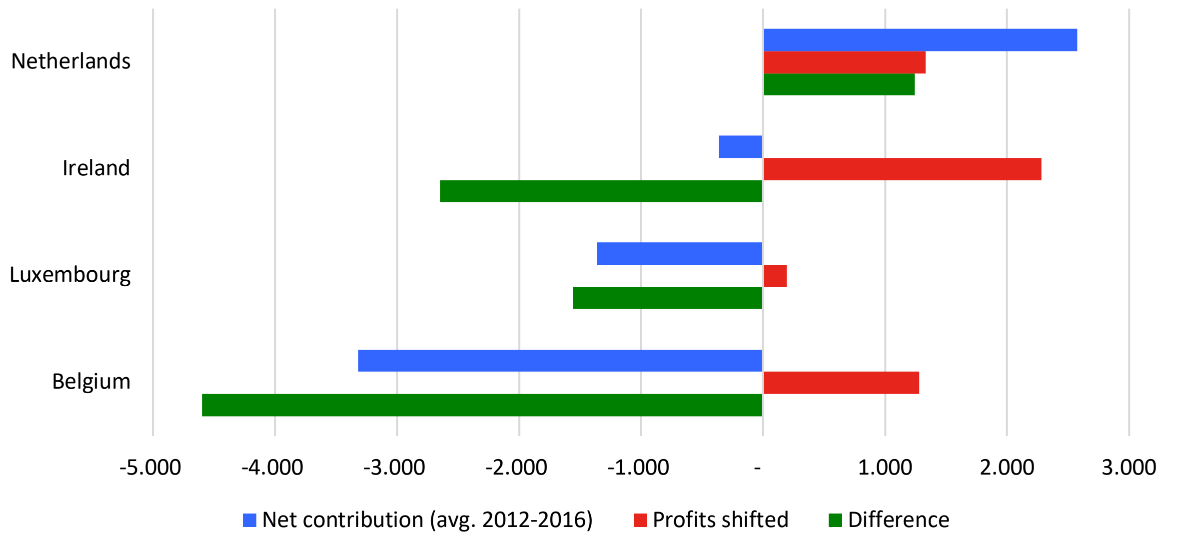


Source: Zucman et al. (2018), own projections

- ***The costs of the EU for the EU6 (national perspective)***

Third, we subtract the gains of profit shifting from the net contributions of the EU tax havens, while adding the losses to the national contributions of the EU22. This would give a more accurate picture on their *de facto* net contributions and net receipts.

Figure 5. Revised net costs for four tax havens (mio EUR)



Source: Zucman et al. (2018), own projections

Figure 5 shows that the *de facto* net contributions (net receipts) to the EU would decrease (increase) significantly for the main EU tax havens. The net contribution of the Netherlands, for instance, would be more than halved from 2.6 to 1.2 billion euro, while the net receipts of Ireland would increase dramatically from 0.4 to 2.6 billion euro. Also the net receipts for Luxembourg and Belgium - already large net recipients by hosting several EU institutions - would increase.

Political assessment

One of the main features of the EU budget is that it contributes to a redistribution of wealth, which enables among other things some of its most deprived areas to catch up with the most advanced regions. The (al)location of European institutes and agencies is also important. Especially the rich member states Belgium and Luxemburg benefit from this. That the Brexit leads to a relocation of the European Banking Authority to Paris and the European Medical Agency to Amsterdam benefits France and the Netherlands respectively. But these benefits are small when compared to the net budget contributions of the two countries. This does not hold the intra-EU redistributions, as result of profit shifting among member states: these are highly relevant for the calculation the net contribution to the European Union. These redistributions favour the smaller and rich EU tax havens and come at the expense of the larger member states.

It appears that the larger member states bear the largest part of the 42.8 billion euro in lost tax revenues from internal profit shifting. For Germany and France who lose 11.8 and 7.7 billion euro in revenues, the net contributions would become twice as high. In addition, for the United Kingdom and Italy who lose 9.3 and 5.9 billion euro in revenue, the net contributions would be even doubled. And the loss of 3 billion euro for Spain would almost offset their net receipt.

Belgium, Ireland, Luxemburg and the Netherlands impose significant costs on other member states through profit shifting. These costs dwarf by far the net contributions to the EU budget by these four member states. Taking into account the benefits from European institution and agencies, three of them are already a net cost to the European Union. The Netherland is however a net contributor to the EU budget, but imposes in fact net costs on the Union as a whole: 11.2 billion euro.

The benefit for the EU tax havens themselves is rather limited. Their strategy - levying low tax rates over an enormous artificial tax base - not only steels away tax revenues from neighbours, it fails to capture much of the loot (a mere 5.1bn over a base of 163bn). The rest of the loot ends in the hands of shareholders and corporate bigwigs like Jeff Bezos and Mark Zuckerberg. This is clearly at odds with the EU principle of good-neighbourliness and solidarity, and exacerbates inequality across the EU.

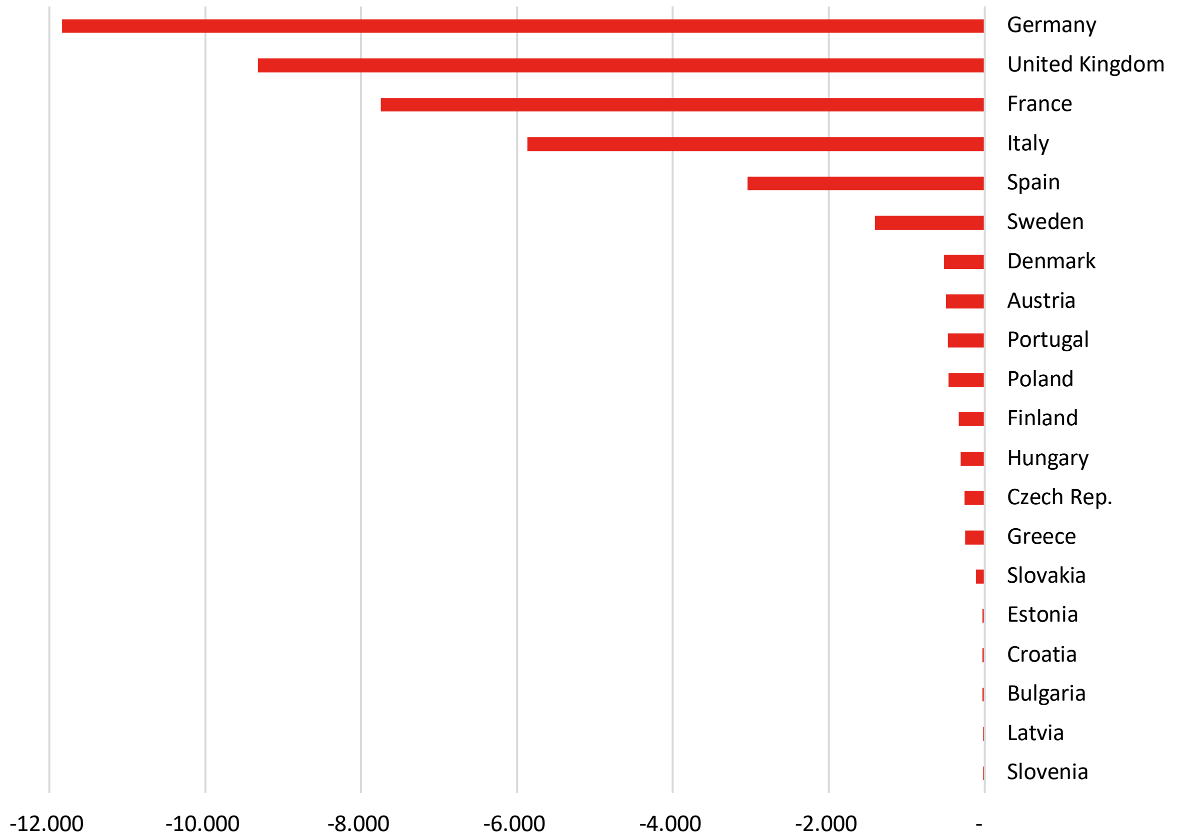
Therefore, the authors would support an overhaul of the corporate tax system in the European Union. The recent proposal for a common consolidated corporate tax base, supported by a large majority in the European Parliament, renders internal profit shifting obsolete. Furthermore, Emmanuel Macron has proposed to establish a binding rate range for corporate taxation in the EU “because members cannot enjoy European solidarity and play against the others at the same time”[5]. However, these measures require unanimity in council, which means they will also need the support of the six EU tax havens. The good news is that pressure is mounting on these countries, and one possible suggestions to apply even more pressure is to explore the idea of enhanced corporation in corporate taxation, which will shield participating countries from intra-EU profit shifting. In fact, the negotiations on the EU budget and on the European corporate tax system should go in hand in hand.

[5] Sorbonne speech

There is no good reason that a country like the Netherlands can claim it contributes to the EU; in fact, the country imposes a significant cost on its European partners.

Appendix

Figure A. Foregone tax revenues EU22 (m EUR)



Source: Zucma