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Key drivers of EU budget allocation: Does power matter?

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ABSTRACT

We examine the determinants of the EU budget allocation among Member States. In line with the analysis by Kauppi and Widgrén (2004) we test two alternative explanations: political power vs. "needs view" . To do so, we extend the original data set (1976–2001) up to 2012 and introduce alternative econometric specifications. We also put forward the nucleolus as a measure of political power in the distributive context. Our results demonstrate that both power and "needs" are important factors in explaining EU budget allocation. Political power matters, but not as much as previous studies have shown. We also conclude that the nucleolus is a good alternative to the Shapley–Shubik index which was used previously. Power is more balanced with needs under the specifications based on the nucleolus.

1. Introduction

In 2013, the European Union (EU) expenditure budget was around €149 billion. Of this, resources for cohesion had a share of 46.8% followed by agricultural and environmental resources with 39.8%. Due to the magnitude of the budget, its distribution between different member countries is a crucial political issue. Along these lines, we investigate the relative importance of the main factors that have been argued to explain budget shares.

Previous literature (Anderson and Tyers, 1995; Courchene et al., 1993; Kandogan, 2000; Kauppi and Widgrén, 2004, 2007; Tangermann, 1997) has tested two alternative explanations of the EU budget distribution across the member states. The first is a "needs view", which states that the budget allocation is determined by the principle of solidarity. According to this hypothesis, the countries with a relatively large agricultural sector and/or a relatively worse economic situation emerge as the major recipients of the EU budget. In fact, some of the previous studies have focused exclusively on this explanation (Anderson and Tyers, 1995; Courchene et al., 1993; Tangermann, 1997). The second explanation is that the budget allocation across the members

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reflects the distribution of their political power. Thus, those countries with more power in the allocation process arguably receive larger shares of the budget.

Some studies investigate both the needs and the power views (Aksoy, 2010; Kandogan, 2000; Kauppi and Widgrén, 2004, 2007). In particular, the empirical analysis by Kauppi and Widgrén (2004) reveals the strong prevalence of political power motives. Their results indicate that political power matters much more than needs when determining the allocation of budget expenditures among EU member states.

The overall purpose of this paper is to reconsider the analysis of Kauppi and Widgrén (2004) and to challenge their conclusions. To do so, we extend the original data set (1976–2001) up to 2012 and introduce alternative model specifications. In contrast to the existing studies which have used the Shapley– Shubik index as a measure of political power, we also employ a different measure: the nucleolus. It has been argued that the nucleolus is an appropriate power measure in distributive situations as well as a good alternative to traditional measures such as the Shapley– Shubik index.[1] Moreover, we apply econometric techniques which are more suitable for the analysis at hand than those used previously.

The paper is structured as follows. Section 2 provides a brief introduction to the EU budget, including the processes of designing and allocating EU expenditures and revenues. In Section 3 we discuss the theoretical properties of two different power indices. Specifically, we highlight the advantages of the nucleolus over other indices in distributive situations. In Section 4 we specify a simple empirical model in order to determine the key drivers of EU budget allocations. Section 5 concludes with a summary of the main findings and discusses some policy implications.

2. EU budget: procedure and evolution

As mentioned in the Introduction, the EU expenditure budget represents a significant amount of resources. In 2013, total expenditures were €148,468 million. Although this is not a substantial amount in relative terms (just 1.13% of the EU-27 Gross National Income, GNI), some crucial policies were developed using EU funding. Examples are the Common Agricultural Policy (now part of a more extensive section on the preservation and management of natural resources) and several policies oriented towards the economic development of designated target regions (cohesion and competitiveness policies). Each EU member has to contribute to the EU budget by means of GNI-based resources (74.3%), VAT-based own resources (9.5%), and traditional own resources (TOR, 10.4%).

In 1976, the EU expenditure budget amounted to only €7563 million; it is clear that the EU budget has grown substantially over the last four decades.[2] This increase reflects both the history of EU integration and several budgetary reforms. In 1986, the EU expanded from 10 to 12 countries due to the integration of Portugal and Spain as new members. Similarly, Austria, Finland and Sweden joined the EU/EC in 1995. Furthermore, one of the largest phases of expansion occurred in 2004, when the EU went from 15 to 25 member countries.[3]

Successive reforms have also changed the structure of the EU budget. At the Brussels European Council in February 1988, a political agreement on doubling, in real terms, the budget of the Structural Funds between 1987 and 1993 was reached. Subsequently, Member States agreed at the Edinburgh European Council in December 1992 that the budget for structural operations would be further increased, specifically for the cohesion countries (Greece, Ireland, Portugal and Spain). Also in Edinburgh, Member States decided to strengthen some particular policies such as research and development, external actions and financial aid to Central and Eastern European countries. The basis of more stringent budgetary discipline was established in the Agenda 2000 agreements.

The European Commission, the Council and the Parliament all participate in the budget process. However, over the past decades the role of each institution, as well as the voting rules, have undergone a number of changes (Kauppi and Widgrén, 2007). The relationship between the Council and the Parliament was controversial until the 1992 Edinburgh meeting, where an Interinstitutional Agreement was established in order to facilitate the process of making budgetary decisions.

The budget elaboration process involves the following steps. First, based on the multi-annual financial framework in force and the budgetary guidelines for the coming year, the European Commission prepares a preliminary draft budget. During this stage, spending priorities are established, caps or ceilings on the maximum growth rate of different budgetary sections are imposed and the total budget is decided.

Once a preliminary draft has been drawn up, the European Commission submits it to the Council and the Parliament. The budgetary authority, comprising both institutions, amends and subsequently adopts the draft budget. The Council is then expected to adopt its position on the preliminary draft budget proposed by the Commission, elaborate and approve a definitive draft budget. Next, the Parliament can modify the draft, by adopting amendments to the Council's position, or by proposing some amendments to particular expenses. The final proposed document is then approved by simple majority by the Parliament. Following this, the Council carries out a second reading of the budget, adopting it by a larger majority than that required at the Parliament.[4] A second reading by the Parliament and the definitive adoption marks the end of the process.

1 See Montero (2005, 2013) and Le Breton et al. (2012) among others.
2 Figures on the EU budget are available at http://ec.europa.eu/budget/figures/index_n.cfm.
3 The new members were the Czech Republic, Cyprus, Slovak Republic, Slovenia, Estonia, Hungary, Latvia, Lithuania, Malta and Poland.
4 Usually, at least a qualified majority is required to adopt budgetary decisions at the Council.