HM Treasury

European Union Finances 2020:

Statement of the 2020 EU Budget and measures to counter fraud and financial mismanagement

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Presented to Parliament by

the Chief Secretary to the Treasury

by Command of Her Majesty

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Contents

1. Chapter 1

Introduction

1.1 In 1980, following a recommendation by the Public Accounts Committee (PAC), the government agreed to present an annual statement (statement) to Parliament giving details of the Budget of the European Union (EU Budget).

1.2 This statement is the 40th in the series, and the last which will cover the UK's membership of the EU. The UK left the EU on 31 January 2020 following the Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community, (the Withdrawal Agreement) signed on 24 January.[1]

1.3 The Withdrawal Agreement was followed by a transition period in which the UK was no longer a member of the EU but remained a member of the single market and customs union. During that time, it continued to be subject to EU rules and obligations to contribute to the EU Budget. Accordingly, this statement covers the one month that the UK was a member of the EU and the eleven months of the transition period.

1 https://www.gov.uk/government/publications/new-withdrawal-agreement-and-political-declaration

1.4 First, it describes the EU Budget for 2020. It then sets out details, including some forecasts, of the United Kingdom's gross and net contributions to the EU Budget over the calendar years 2013 to 2020. Details of recent developments in EU financial management and the fight against fraud affecting EU funds are also provided, as is an update on the UK's strategy for using EU funds and minimising disallowance.

1.5 While most of the statement is backward-looking, it contains two annexes which provide information on current engagement with the EU on the implementation of the Withdrawal Agreement and the Trade and Cooperation Agreement. These annexes provide context for the next edition of the statement, which will report on implementation of these agreements during 2021.

1.6 Annex E provides the following additional information:

- a summary of the first payment request of UK net liabilities made by the EU under the Withdrawal Agreement, which will be reported in full in next year's statement
- an explanation of the UK's strategy for assurance of the financial provisions of the Withdrawal Agreement
- a summary of the technical engagement between the UK and the EU on implementation of the

financial provisions, and the formal governance of that relationship

- an analysis of the financial settlement under the EU Withdrawal Agreement, including an updated estimate of the financial settlement and details of applicable assurance arrangements now that the UK has left the EU

1.7 Annex F provides an update on UK participation in programmes under the Trade and Cooperation Agreement (TCA).

2. Chapter 2

Expenditure

2.1 The Multiannual Financial Framework (MFF) sets ceilings for each EU Annual Budget. The current MFF covers the period 2014-20. It was agreed in 2013 and achieved a real terms cut in the payment ceilings for the first time. The 2020 commitment appropriations ceiling was €168.8 billion (£143.6billion)[2] and the payment appropriations ceiling was €172.4 billion[3] (£146.7 billion). Prescribed flexibilities available within the budgetary system enable proposals for the overall level of commitments to be higher than the relevant ceiling. Further information explaining the difference between payment and commitment appropriations can be found in the Glossary.

The 2020 EU Budget

2.2 The EU financial year runs from 1 January to 31 December. The 2020 EU Budget for commitment and payment appropriations was agreed under the Romanian Presidency of the EU[4] in the

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2 2020: £1 = €1.175364. This is the 31 December 2019 exchange rate, which is the rate at which all UK VAT-based and GNI-based contributions, and the UK rebate, were converted to sterling throughout 2019.

3 Draft general budget of the European Union for the financial year 2020: http://eur-lex.europa.eu/resource.html?uri=cellar:064b4bf7-76ef-11e9-9f05-01aa75ed71a1.0001.02/DOC_2&format=PDF

4 Council decision determining the order in which the office of President of the Council shall be held: https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32007D0005

second half of 2019[5]. Negotiations began in June 2019, when the Commission proposed a draft EU Budget for 2020[6]. This proposed total commitment appropriations of €168.3 billion (£143.2 billion) and payment appropriations of €153.6 billion (£130.7 billion) in EU spending (nominal figures). The Commission amended its proposal in October 2019, on the basis of new information, such as updates to expenditure and revenue. On this occasion, these updates did not significantly change the overall figures for commitment and payment appropriations[7].

2.3 The Council adopted its position in July 2019, proposing to reduce the Commission's original proposal to €166.8 billion (£141.9 billion) in commitment appropriations and €153.1 billion[8] (£130.3 billion) in payment appropriations. In October 2019, the European Parliament provided its position, which would have set the level of EU spending in 2020 to €170.9 billion (£145.5 billion)

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5 Deal reached on 2020 EU budget https://www.consilium.europa.eu/en/press/press-releases/2019/11/18/2020-eu-budget-council-and-parliament-reach-agreement/

6 Commission proposes draft EU budget 2020: https://ec.europa.eu/commission/presscorner/detail/en/IP_19_2809

7 Amending letter no.1 to the draft general budget 2019: https://ec.europa.eu/info/sites/default/files/about_the_european_commission/eu_budget/documents/com487final_-_en_-_al1-2020_explanatory_memorandum.pdf

8 EU Budget 2020: Council sets out its position: *https://www.consilium.europa.eu/en/press/press-releases/2019/07/10/2020-eu-budget-council-agrees-its-position/* ; Draft general budget of the European Union for the financial year 2020: Council position of 8 July 2019: *https://data.consilium.europa.eu/doc/document/ST-10919-2019-INIT/en/pdf*

in commitment appropriations and €159.1 billion[9] (£135.4 billion) in payment appropriations.

2.4 The Council and European Parliament reached agreement on 27 November.[9] The adopted 2020 EU Budget provided for commitment appropriations of €168.7 billion (£143.5 billion) and for payment appropriations of €153.6 billion (£130.7 billion).[10] The payment appropriations for each of the main EU Budget headings are shown in Table 2.A: 2020 EU Budget.

2.5 Table 2.A also shows various stages of the negotiations during 2020. Figures for previous years' EU Budgets are provided for comparison in Annex C (Tables C.1 and C.2).

2.6 Following a series of budget amendments – in-year expenditure and revenue changes to the adopted EU Budget during the year of implementation – a total of €5.1 billion of commitment appropriations and €9.0 billion of payment appropriations were added to the adopted 2020 EU Budget, mainly due to the EU's economic response to Covid-19 over the course of 2020.

9 ;_European Parliament resolution of 15 October 2019 on the Council position on the draft general budget of the European Union for the financial year 2020: *https://www.europarl.europa.eu/doceo/document/A-9-2019-0017_EN.html*

10 Definitive adoption of the European Union Budget for the Financial Year 2020: *https://eur-lex.europa.eu/budget/data/General/2020/en/GenRev.pdf*

2.7 This left a final agreed 2020 EU Budget of €173.8 billion (£147.9 billion) in commitment appropriations and €162.5 billion[11] (£138.3 billion) in payment appropriations. Further details on budget amendments and the final agreed 2020 EU Budget can be found in Box 2.A.

Box 2.A: Budget Amendments and the Final Agreed 2019 EU Budget

2.8 The final agreed 2020 EU Budget of €162.5 billion in payments is within the 2019 payments ceiling agreed in the 2013 MFF deal of €172.4 billion.

2.9 Table 2.A shows payment appropriations for the adopted 2020 EU Budget. This is the original 2020 EU Budget which was formally agreed by the Council and European Parliament in November 2019. This is prior to any in-year budget amendments.

2.10 Table 2.A also shows the final agreed 2020 EU Budget. This includes the effects of draft amending budgets 1-9 approved by the Council and European Parliament. Draft amending budgets are proposals made by the Commission to amend certain aspects of the adopted Budget of a year. These can increase or decrease expenditure in line with updated forecasts of expenditure and revenue. They can also adjust member state

11 Amending budget No. 9/2020 *https://www.europarl.europa.eu/RegData/docs_autres_institutions/commission_europeenne/com/2020/0961/COM_COM(2020)0961_EN.pdf*

contributions. In total, the final agreed 2020 Budget was €9.0 billion in payment appropriations higher than when adopted, primarily due to mobilisation of the European Union's economic response to Covid 19.

2.11 Chart 2.A shows the payment appropriations by heading for the final agreed 2020 EU Budget.

2.12 The final agreed 2020 EU Budget will be referred to in the text, used in tables and displayed in charts throughout this document, unless stated otherwise.

Table 2.A: Table 2.A: 2020 EU Budget (€ million nominal)

Payment Appropriations	Financial Perspective Ceiling[1]	Commission draft 2020 EU Budget[2]	Council position[2]	European Parliament position[2]	Adopted 2020 EU Budget[3]	Final Agreed 2020 EU Budget[4]	Final Agreed 2019 EU Budget[5]
1. Smart and Inclusive Growth of which:		72,151	72,011	77,229	72,354	77,454	67,557
1a. Competitiveness for Growth and Jobs		22,109	22,004	23,998	22,308	22,308	20,522
1b. Economic, Social and Territorial Cohesion		50,042	50,007	53,231	50,046	55,146	47,035
2. Sustainable Growth: Natural Resources		58,014	57,774	58,178	57,904	57,904	57,400
3. Security and Citizenship		3,724	3,689	3,823	3,685	6,369	3,527
4. Global Europe		8,986	8,946	9,135	8,929	9,112	9,358
5. Administration		10,327	10,272	10,364	10,275	10,274	9,945

Total Payment Appropriation	172,420	153,621	153,112	159,146	153,566	162,539	148,492

Note: Column totals do not equal the sum of individual items due to rounding and spending not attributable to any heading e.g. despite having the same item values, the difference between the total payment appropriations for the adopted and final 2019 budgets can be explained by an increase of €294 million under the Flexibility instrument.

1 Draft general budget of the European Union for the financial year 2020: https://www.europarl.europa.eu/RegData/docs_autres_institutions/commission_europeenne/com/2020/0961/COM_COM(2020)0961_EN.pdf

2 Commission draft 2020 Budget: https://eur-lex.europa.eu/budget/data/DB/2020/en/SEC00.pdf

3 Final Adopted Budget: https://eur-lex.europa.eu/budget/data/General/2020/en/GenRev.pdf

4 Draft amending budget No.9/2020: https://www.europarl.europa.eu/RegData/docs_autres_institutions/commission_europeenne/com/2020/0961/COM_COM(2020)0961_EN.pdf

5 Draft amending budget No. 3/2019: https://op.europa.eu/en/publication-detail/-/publication/fdfda29d-7c70-11e9-9f05-01aa75ed71a1/language-en

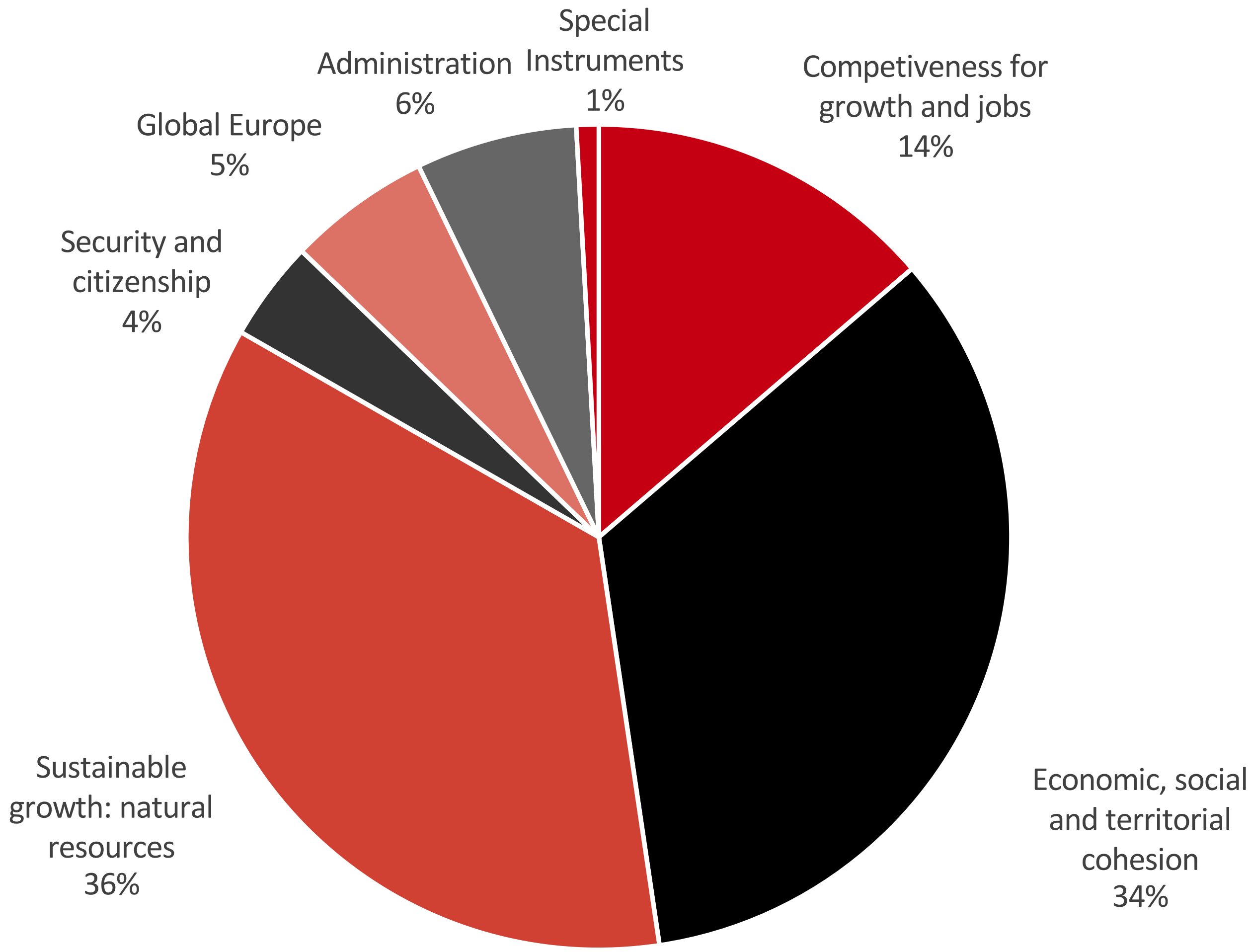
2.13 Details of the levels of payments in the final agreed 2020 EU Budget are as follows (all figures are nominal):[12]

- **Heading 1: Smart and Inclusive Growth.** Expenditure in this area includes research and development, education and training, employment and social policy. Payments for Heading 1 overall were set at €77.5 billion (£65.9 billion)
- **Payments towards research, learning, and innovation (Heading 1a)** were set at €22.3 billion (£19.0 billion). Payments toward fostering regional growth and employment (Heading 1b) were set at €55.1 billion (£46.9 billion)
- **Heading 2: Sustainable Growth: Natural Resources.** Expenditure in this area includes spending on the Common Agricultural Policy, fisheries, rural development, and measures aiming to contribute to food quality and a cleaner environment. Payments in this area were set at €57.9 billion (£49.3 billion)
- **Heading 3: Security and Citizenship.** Expenditure in this area includes immigration, migration, security, and fundamental rights and justice. Payments for Heading 3 overall in 2020, excluding those associated with the European Union Solidarity Fund, were set at €6.4 billion (£5.4 billion).

12 Draft amending budget No. 3/2019 (includes amending budgets 1-3): https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019B1818&from=EN

- **Heading 4: Global Europe.** Expenditure in this area is focused on EU foreign policy and international development. Payments for Heading 4 were set at €9.1 billion (£7.8 billion)
- **Heading 5: Administration.** Expenditure for Heading 5 is on the functioning of the EU institutions and includes remuneration and allowances for staff and members, pension costs, and rent and other building costs. Payments for 2019 under Heading 5 were set at €10.3 billion (£8.7 billion)

Chart 2.A: Final Agreed 2020 EU Budget – payment appropriations by budget heading



Source: Amending Budget No.9/2020:

https://www.europarl.europa.eu/RegData/docs_autres_institutions/commission_europeenne/com/2020/0961/COM_COM(2020)0961_EN.pdf

3. Chapter 3

Contributions to the EU Budget

EU Revenue

3.1 The Own Resources Decision provides for three sources of EU revenue: customs duties and sugar levies which together are known as Traditional Own Resources (TOR); contributions based on VAT; and GNI-based contributions. A more detailed explanation can be found in the Glossary.

3.2 Chart 3.A shows a breakdown of how the 2020 EU Budget was financed by EU member states. The key points to note for the 2020 EU Budget are[13]:

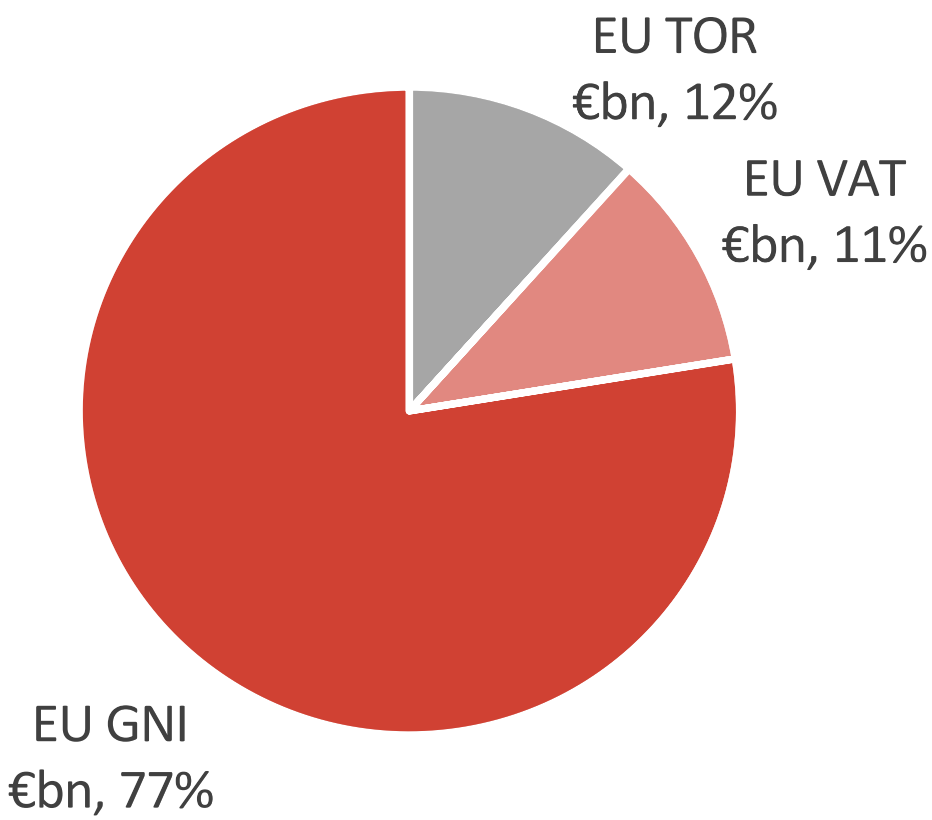
- TOR is €18.5 billion (£15.6 billion) and the UK's share is 15.1%. In 2019, outturn revenue from this source was €21.4 billion (£19.1 billion), of which the UK's share was 14.5%
- VAT-based contributions are €17.3 billion (£14.8 billion) and the UK's share is 19.1%. In 2019, total VAT-based contributions were €18.1 billion (£16.2 billion), of which the UK's share was 18.1%

13 Estimates are sourced from the European Commission's Amending Budget 9 to the 2020 budget. https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32021B0118&from=EN. Outturns are sourced from the European Commission's 2019 EU Budget Financial Report. https://ec.europa.eu/info/strategy/eu-budget/long-term-eu-budget/2014-2020/spending-and-revenue_en

- GNI-based contributions are €124.0 billion (£105.5 billion) and the UK's share is 15.6%. In 2019, GNI-based contributions were €105.4 billion (£94.3 billion) with a UK share of 15.1%
- the estimated value of the UK's rebate in 2020 is €6.1 billion (£5.2 billion) compared with €5.1 billion (£4.6 billion) in 2019. A detailed explanation of how the UK rebate is calculated, and how it operates, can be found in the Glossary

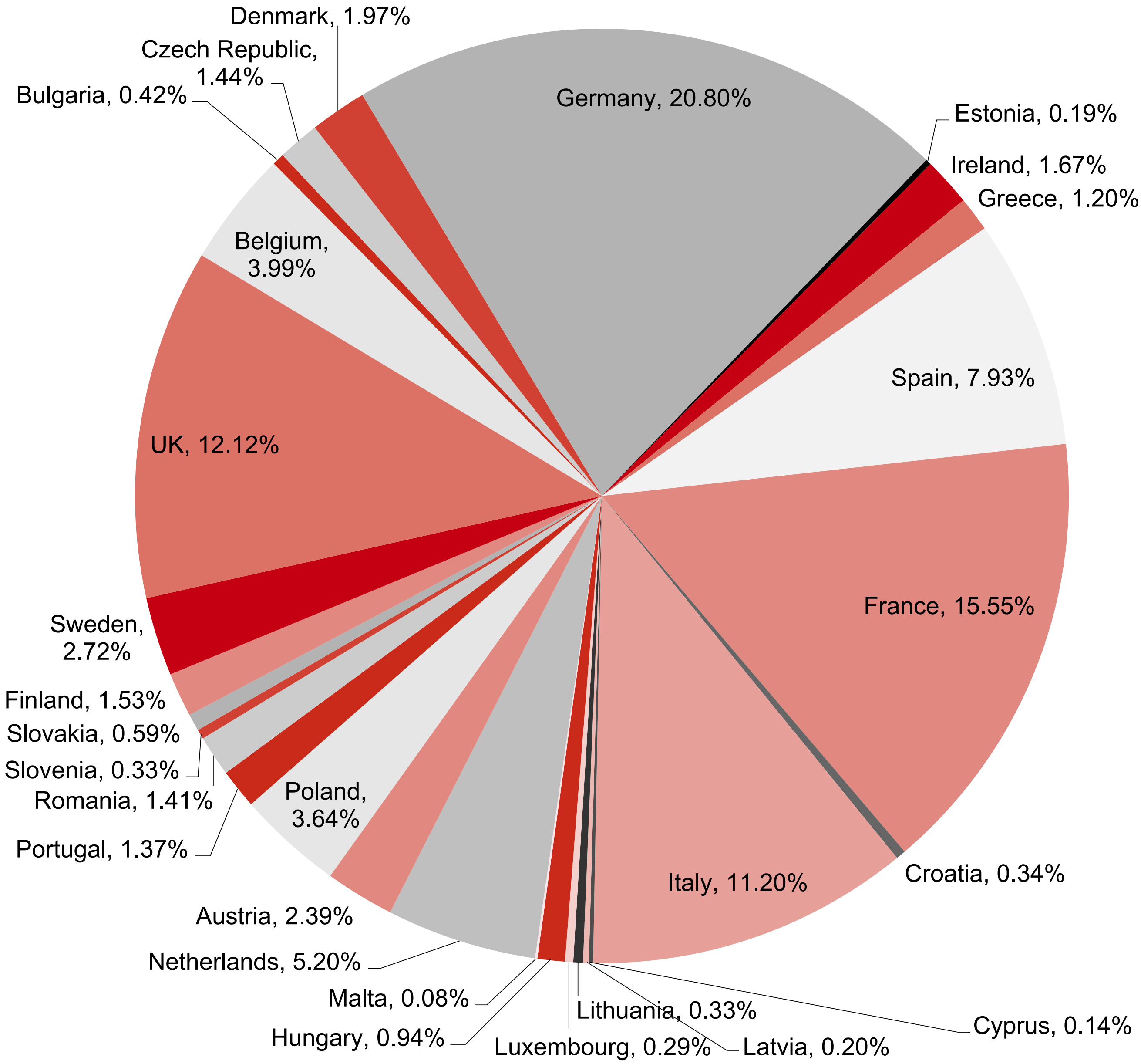
3.3 Chart 3.B shows each member state's share of financing the 2020 EU Budget after taking account of the UK rebate.

Chart 3.A: 2020 EU Budget Revenue



Source: Amending Budget No. 9 to the 2020 Budget, European Commission.
https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32021B0118&from=EN

Chart 3.B: EU Budget revenue 2020 – percentage share after rebates by member states



Source: Amending Budget No. 9 to the 2020 Budget, European Commission.
https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32021B0118&from=EN

The UK's net contribution

3.4 Table 3.A shows the UK's gross payments, rebate, public sector receipts and net public sector contributions to the EU Budget for calendar years 2014 to 2020. The figures for 2020 include estimates. Figures for earlier years are outturns.

Table 3.A: Gross payments, rebate and receipts (calendar years)

							£ million
	2014	2015	2016	2017	2018	2019	2020
Gross contribution[1]	18,778	19,560	16,996	18,625	17,445	18,946	22,244
Less: UK rebate	-4,416	-4,914	-3,878	-5,633	-4,247	-4,516	-5,201
Less: Public sector receipts	-4,583	-3,883	-3,493	-4,084	-4,279	-5,022	-4,461
Net public sector contribution[2]	9,779	10,763	9,625	8,909	8,919	9,408	12,583

1 Gross payment figures include Traditional Own Resources payments at 75% up to September 2016 and 80% thereafter. The remainder is retained by the UK. The UK's gross payments are automatically corrected to account for the rebate, meaning the UK only pays the post-rebate amount.

2 Due to rounding, totals may not exactly correspond to the sum of individual items.

Source: HM Treasury calculations

3.5 The fluctuation in the UK's net public sector contribution to the EU Budget is due to the nature of the Own Resources system, and consequential fluctuations in the UK rebate, as well as variations in public sector receipts and the exchange rate. For further details, refer to the technical annex and the Glossary.

3.6 UK public sector receipts in 2020, mainly from the European Agricultural Guarantee Fund (EAGF), European Agricultural Fund for Rural Development (EAFRD) and the Social and Regional Development Funds, are worth around £4.5 billion. The majority of these receipts will either be paid to, or used in support of, the private sector but are channelled through government departments or agencies.

3.7 The EU makes some payments directly to the private sector, for example to carry out research activities. These payments do not appear in public sector accounts. It is estimated that in 2019 these receipts were worth £1.7 billion (see Technical Annex B). These payments are not included in Table 3.A or Tables 3.C-D, which provide data only on receipts channelled through the public sector.

3.8 The Commission also publish outturn data on all member states' contributions to the EU Budget and their receipts in previous years. These give a figure for the UK's net contribution that is different from the numbers derived from the OBR's forecasts and UK data. The main reason for this difference is that the Commission's numbers take into account all of the UK's receipts and include those that go directly to UK-based recipients, such as funding for research paid directly to UK universities. Further detail is provided in Annex B.

3.9 Table 3.B sets out the Commission figures for the UK's gross contributions and receipts and the implied net contribution. They are taken from the Commission's latest financial report.

Table 3.B: EU Commission Financial Report data (calendar years)

				£ billion / € billion
	Gross contribution post rebate (€ billion)	Total public and private receipts (€ billion)	Net contribution (€ billion)	Net contribution (£ billion)
2015	21.41	7.46	13.95	10.13
2016	16.62	7.05	9.57	7.84
2017	13.76	6.33	7.43	6.51
2018	16.40	6.63	9.77	8.64
2019	17.15	7.64	9.51	8.35
Average	**17.07**	**7.02**	**10.05**	**8.29**

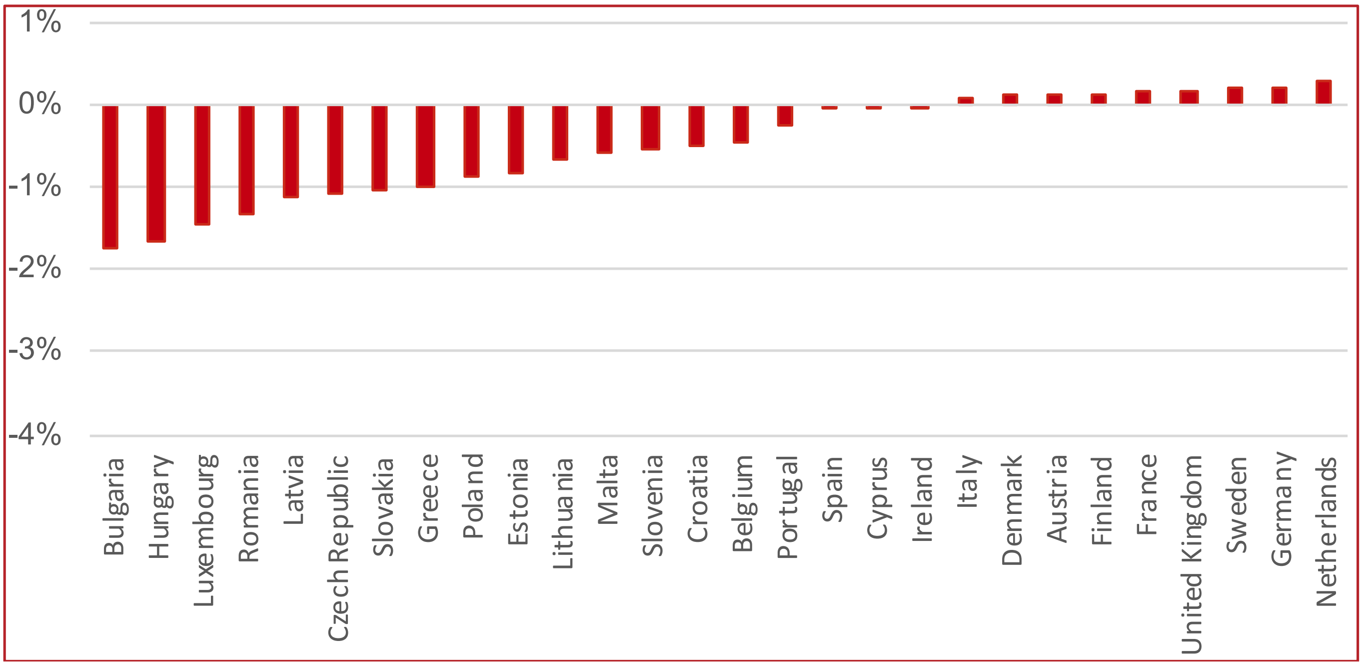
Source: 2019 EU Budget Financial Report, European Commission

3.10 Figures for 2018 include a redistribution of total contributions across the member states following the implementation of the 2014 Own Resources Decision agreed in 2013 as part of the 2014-20 MFF agreement. The new Decision required ratification by all Member States in accordance with their own constitutional requirements before it could enter into force. The Decision was ratified by the UK Parliament through the EU (Finances) Act 2015. The redistribution has been fully anticipated in OBR forecasts since December 2013.

3.11 In accordance with a commitment to the Public Accounts Committee (PAC), the technical annex of this document explains the main differences in respect of calendar years 2017 and 2018 between the government's figures and those which can be derived from the European Commission's EU Budget Financial Reports.

3.12 Chart 3.C shows how the UK's net position compares with those of other member states.

Chart 3.C: Average net contribution as % of GNI by country for the years 2014-2019 by country for the years 2014-2019



Source: 2019 EU Budget Financial Report, European Commission.

Financial year transactions

3.13 The EU financial year runs from 1 January to 31 December, whereas the UK's runs from 1 April to 31 March. Table 3.C gives a breakdown of the UK's transactions with the EU on a UK financial year basis between 2014-15 and 2019-20.

3.14 Under the terms of the financial settlement, the UK continued to participate in the EU budget for 2020. Under the EU budgetary system, payments are scheduled on a monthly basis, but the Commission can request earlier contributions from member states of VAT-based and GNI-based contributions and the UK rebate, to take account of frontloaded

Common Agricultural Policy (CAP) or European Structural and Investment Funds payments, which take place in the first months of the calendar year. From the beginning of 2021, a new payment mechanism was introduced under the Withdrawal Agreement. More information on the Withdrawal Agreement payment mech

Table 3.C: Gross contribution, rebate and public sector receipts (financial years – outturn)

£ million

	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Gross contribution[1]	18,733	17,635	16,926	17,450	20,377	18,355
Less: UK rebate	-4,811	-4,068	-4,757	-4,547	-4,846	-4,149
Less: Public sector receipts	-4,690	-2,810	-4,083	-4,130	-4,378	-5,059
Net public sector contribution[2]	9,232	10,757	8,086	8,773	11,154	9,147

1 Gross payment figures include Traditional Own Resources payments at 75% up to September 2016 and 80% thereafter. The remainder is retained by the UK. The UK's gross payments are automatically corrected to account for the rebate, meaning the UK only pays over the gross post-rebate amount.

2 Due to rounding, totals may not exactly correspond to the sum of individual items.

Source: HM Treasury calculations

Table 3.D: Public sector receipts from the EU Budget (financial years – outturn)

						£ million
	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
EAGF	2,513	1,318	3,057	2,728	2,835	2,783
EAFRD	393	619	367	536	551	735
Social Fund	371	542	268	223	177	901
Regional Development Fund	1,308	297	237	337	752	550
Other Receipts	105	34	153	306	64	89
Total	4,690	2,810	4,083	4,130	4,378	5,059

Source: HM Treasury calculations

4. Chapter 4

Financial Management and anti-fraud issues

4.1 This chapter provides an overview of the annual reports – relating to financial management and anti-fraud issues – published in 2019 and concerning the 2018 EU budget.[14] First, the European Court of Auditors (ECA) annual report that holds the Commission and member states to account for their management of the EU Budget. This report assesses the implementation of the EU Budget and identifies examples of irregular management or expenditure. Second, the Commission's annual 'Fight Against Fraud' report details the actions taken by the Commission and member states to counter fraud affecting EU funds. The report also highlights areas that are most at risk of fraud and in need of targeted action at both EU and national level. Third, the European Anti-Fraud Office (OLAF) annual report, which summaries the activities of the Office during the preceding year. This chapter provides an overview of the annual reports – relating to financial management and anti-fraud issues.

14 The 2019 reports, concerning the 2018 EU budget, are scrutinised here to account for the completion of the EU budget discharge process in 2020

European Court of Auditors' annual report on the 2018 EU Budget

4.2 The ECA is the EU's independent auditor and is responsible for assessing the accounts and payments of EU institutions. The ECA is required to provide the European Parliament and Council with an annual report on the implementation of the EU Budget[15]. This report's purpose is twofold: firstly, to assess the reliability of the EU budget accounts under internationally accepted accounting standards for the public sector; and secondly, to assess the legality and regularity of the underlying transactions in relation to the applicable EU laws and regulations. The report also contains targeted recommendations to address identified errors and weaknesses. It includes a Statement of Assurance (usually referred to as the 'DAS', from the French 'Déclaration d'Assurance') which confirms whether the EU accounts are complete and accurate, and whether income and expenditure have been managed in accordance with all contractual and legal obligations. The report forms an essential element in the European Parliament's oversight of the Commission's management of the EU Budget.

4.3 The ECA's report also launches the annual 'discharge' process, the procedure whereby the

15 The European Court of Auditors' annual report on the 2018 EU Budget can be found at: https://www.eca.europa.eu/Lists/ECADocuments/annualreports-2018/annualreports-2018_EN.pdf

European Parliament, acting on a recommendation from the Council, decides whether to release the Commission from its responsibility for the management of the Budget for the year in question.

4.4 The ECA's report on the 2018 EU budget was published on 8 October 2019. As in previous years, it provided an assessment of each EU Budget area and offered conclusions based mainly on: testing the legality and regularity of transactions; the effectiveness of the principal supervisory and control systems governing the revenue or expenditure involved; and a review of the performance of the EU Budget.

ECA's Statement of Assurance

4.5 In the ECA's opinion, the 2018 EU budget accounts were reliable and gave a fair representation of the financial position and the results of operations and cash flows for the year.

4.6 The ECA found EU revenue underlying the 2018 accounts to be legal and regular in all material aspects, as they have done in every year since 2007.

4.7 The ECA found that payments (EU spending) continued to be affected by material error with an estimated error rate of 2.6% for the 2018 EU Budget as a whole, a small increase from 2.4% for the 2017 budget.

4.8 The ECA considers an estimated error rate above 2% to be material. The ECA's estimate of the level of error is not a measure of fraud, inefficiency or waste. It is an estimate of the money that should not have been paid out because it was not used in accordance with the relevant rules and regulations. This can include payments for expenditure which was ineligible or for purchases without proper application of public purchasing rules.

4.9 All individually assessed areas of EU spending[16] were affected by material error with the exception of administrative expenditure. High-risk expenditure (mainly spending on a reimbursement basis) had an estimated error rate of 4.5%. Low-risk expenditure (mainly made on an entitlement basis) was not affected by material error. The ECA did not consider the overall error rate pervasive. In light of these findings, for the third consecutive year, the ECA granted a qualified – rather than adverse – DAS with regards to the legality and regularity of the transactions underlying the EU Budget accounts.

4.10 In its report, the ECA provides specific assessments for revenue and expenditure policy groups as follows:

16 The ECA provided a specific assessment of four MFF headings: 'Competitiveness,' 'Cohesion,' Natural Resources,' and 'Administration.'

- **Chapter 2 – Budgetary and Financial Management:** This covers the key budgetary and financial management issues which arose in 2018. These include overall levels of spending, the relationship with budgetary and MFF ceilings, levels of unpaid payment claims, and levels of outstanding commitments. The ECA recommended that the Commission:
  - take measures to avoid undue pressure on the level of payment appropriations in the first years of the 2021-2027 MFF
  - ensure, as soon as the common provisioning fund is established, effective management and up-to-date monitoring of the EU Budget's exposure to the related guarantees, and base its calculation of the effective provisioning rate on a prudent methodology based on recognised good practice
  - present annually to the budgetary authority the overall amount and the breakdown of funds transferred from the EU Budget for financial instruments managed by the European Investment Bank (EIB) Group
- **Chapter 3 – Getting Results from the EU Budget:** The theme of this chapter is performance. This chapter has three parts: the first on EU Budget performance indicators; the second on the main results of the ECA's 2018 special reports on

performance; and the third on the follow-up of the ECA's recommendations it made in its special reports published in 2015.

- The ECA recommended that the Commission:
- promote the inclusion of improved indicators in the programme statements, which provide more relevant information on the achievements of programmes, clearly link to actions financed by the programmes and cover the programme objectives
- propose performance frameworks for all programmes, unless otherwise justified, with focus on quantitative baselines, targets and milestones to assess progress
- aim to receive timely performance information for all performance indicators, by introducing new reporting tools
- document the targets proposed so that the budgetary authority can assess their level of ambition
- further improve the Programmes' Performance Overview by using one method for calculating progress towards the target and clearly explaining the rationale for using specific indicators

- **Chapter 4 – Revenue:** This covers the revenue through which the EU finances its budget. For 2018 the ECA concluded that the level of error in Member States' payments of TOR, VAT and GNI based resources and other revenue was not material. The error rate for transactions tested was estimated to be free from material error. The examined supervisory and control systems for GNI and VAT-based own resources and other revenue were assessed as, overall, effective. However, some of the examined systems for TOR were assessed as only partially effective. There remain some concerns regarding the calculation of Member States' contributions to the EU budget.
  - The ECA recommended that the Commission:
  - implement a more structured and documented risk assessment for its TOR inspection planning
  - reinforce the scope of its monthly and quarterly checks of TOR A and B account statements
- **Chapter 5 – 'Competitiveness for growth and jobs':** This chapter covers spending on research and innovation, education and training, trans-European networks in energy, transport and telecommunications, space programmes and business development. The ECA found that the error rate in this area was 2.0% (down from 4.2% in 2017). The main source of error was research

spending, through the reimbursement of ineligible costs.

– The ECA recommended that the Commission:

– carry out more targeted checks of small and medium sized enterprises' (SMEs) and new entrants' cost claims, and enhance its information campaigns on the funding rules

– for the next Research Framework Programme, further simplify the rules for calculating personnel costs and assess the added value of the mechanism for large research infrastructure costs and review how its methodology can be improved

– for Horizon 2020, address the observations made in the context of ECA's review of the ex-post audits concerning documentation, sampling consistency and reporting, as well as the quality of the audit procedures

– promptly address the findings of the Commission's Internal Audit Service, concerning the Education, Audio-visual and Culture Executive Agency's (EACEA) Erasmus+ expenditure and the monitoring of compliance with research and innovation projects

- **Chapter 6 – 'Economic, social and territorial cohesion:** This chapter covers spending to reduce development disparities between different Member

States and regions of the EU and strengthening all regions' competitiveness. These objectives are implemented through the European Regional Development Fund (ERDF), the Cohesion Fund (CF) and the European Social Fund (ESF). The ECA identified the most prevalent sources of error as ineligible expenditure and projects, followed by infringement of internal market rules. The overall error rate across this MFF heading area was 5.0% (up from 3.0% in 2017).

- The ECA recommended that the Commission:
- ensure that, for SME Initiative programmes, regular checks, based on a representative sample of disbursements to final recipients, are carried out, at the level of financial intermediaries by an appropriate auditor selected by the EIB Group, or where such checks are insufficient, the Commission develop and implement appropriate control measures to prevent the possibility of material irregular expenditure at closure
- take the necessary steps to ensure that the checklists used by managing and audit authorities include verifications of compliance with Article 132 of the Common Provisions Regulation, which states that beneficiaries must receive the total amount of eligible expenditure

due no later than 90 days from the date of submission to the related payment claim

– address weaknesses and ensure that no programme can be closed with a material level of irregular expenditure

- **Chapter 7 – 'Natural resources':** This spending area covers the CAP, the Common Fisheries Policy (CFP) and some EU spending on environment and climate action. The ECA estimated the error rate as 2.4% (unchanged from the 2017 budget). Direct payments, as a whole, were free from material error, but the error rate remains high in relation to rural development, market measures, the environment, climate action and fisheries.

  – The ECA recommended that the Commission:

  – address weaknesses in CAP performance measurement and reporting for the post-2020 period, by taking account of the weaknesses identified in the current framework, in order to ensure that result indicators properly measure the effects of actions and that they have a clear link to the related interventions and policy objectives

- **Chapter 8 – 'Security and Citizenship':** This chapter covers payments made with the objective of strengthening the concept of EU citizenship by creating an area of freedom, justice and security without internal borders. The ECA does not calculate an error rate for this area as there are too few transactions for it to take a representative sample.

- The ECA recommends that the Commission:
- ensure that, when making administrative checks of payment claims, it systematically uses the documentation it has required its grant beneficiaries to provide, in order to properly examine the legality and regularity of the procurement procedures these beneficiaries have organised
- instruct the Member State authorities responsible for the Asylum, Migration and International Fund (AMIF) and Internal Security Fund (ISF) national programmes to adequately check the legality and regularity of the procurement procedures organised by the fund’s beneficiaries when making administrative checks of their payment claims

• **Chapter 9 – ‘Global Europe’:** This chapter covers spending related to foreign policy and international development. The ECA does not calculate an error rate for this area as there are too few transactions for it to take a representative sample.

- The ECA recommends that the Commission:
- take steps to reinforce the obligation on international organisations to forward the ECA,

at its request, any document or information necessary to carry out its task as foreseen in the Treaty in the Functioning of the EU (TFEU)

- take steps to adapt the Directorate-General for European Neighbourhood Policy and Enlargement Negotiation's (DG NEAR) residual error rate (RER) methodology to limit full-reliance decisions, and that it monitor its implementation closely
- revise the DG for Civil Protection and Humanitarian Aid Operations' (DG ECHO) calculation of the 2019 corrective capacity by excluding recoveries of unspent pre-financing

- **Chapter 10 – 'Administration':** This chapter covers the administrative and other expenditure of EU institutions and bodies. Expenditure in this area includes human resources (salaries, allowances and pensions), which account for c.60% of the spending in this policy group, in addition to expenditure on buildings, equipment, energy, communications and information technology, which accounts for the remainder. The results of the ECA audits of the EU agencies and other decentralised bodies are reported in specific annual reports, which are published separately. The ECA concluded that the level of error for payments was not material.

– The ECA recommended that the Commission:

– should improve systems for managing statutory family allowances by increasing the frequency of checks

Council recommendation to the European Parliament on Discharge

4.11 On 17 February 2020, the Council noted both the ECA's Statement of Assurance on the implementation of the EU Budget for the financial year 2018 and the ECA's analysis of the audit findings and conclusions[17]. The Council stressed the importance of independent audits carried out at EU level and strongly supported the ECA's work and audit findings.

4.12 The Council welcomed that the ECA had given a qualified opinion, rather than an adverse one, on the legality and regularity of payments. However, the Council regretted that the estimated level of error continues to be above materiality and has increased in 2018 (2.6%) compared to 2017 (2.4%). The Council also stated that simplification of rules is key to achieving a lower error rate and invited the Commission and member states to ensure that simplification remains a top priority.

17 https://ec.europa.eu/info/publications/discharge-2018-council-recommendations_en

4.13 In its conclusions responding to the ECA's Statement of Assurance, the Council made a number of recommendations. The Council:

- invited the Commission to carefully monitor the evolution of potential liabilities in the current MFF and to evaluate how to mitigate the EU risk exposure
- called on the Commission to assess performance of EU programmes on the basis of milestones
- urged the Commission to continue its efforts to reach an error rate below the materiality threshold for research spending
- reiterated its appeal to the Commission to continue its efforts to address the causes of error under the "Competitiveness for Growth and Jobs" heading, with a particular focus on the programmes subject to persistently high error levels
- invited the Commission to carry out more targeted checks of new entrants' and SMEs' cost claims under the Horizon 2020 programme, to enhance its information and communication efforts towards providing those beneficiaries with proper guidance on eligibility issues and funding rules, as well as to further simplify the rules for calculating personnel costs in the next Research Framework Programmes
- called on the Commission to continue providing appropriate and consistent training and guidance,

along with sharing good practices to assist beneficiaries and national authorities in the implementation of programmes under the heading "Economic, Social and Territorial Cohesion"

- called on the Commission to improve its procedures to manage staff costs and statutory family allowances

4.14 Sweden and the Netherlands submitted a joint counterstatement, urging the Commission to continue efforts to increase the focus on results and results-based management, and to identify further opportunities to simplify the complex rules and regulatory framework governing EU budget expenditure, whilst inviting the Commission and Member States to increase efforts to promote transparency and reliability of audits.

The European Parliament takes a final decision on whether to discharge the EU Budget

4.15 On 13 May 2020 the European Parliament formally approved the discharge of the EU budget accounts for 2018 and issued their Resolution.[18] It did so having considered the ECA's report, the Commission's response, and the recommendation of the Council.

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18 Discharge 2018: EU general budget 2018 – European Parliament can be found at: www.europarl.europa.eu/doceo/document/TA-9-2020-0271_EN.pdf

Fight against Fraud Report 2018

4.16 The protection of the EU's financial interests and the fight against fraud are areas of shared responsibility between the Commission and member states. Each year, the Commission, in cooperation with member states, issues a report on details of irregularities, the latest statistics on fraud and recent measures taken to reduce irregularities and fraud. This report is required under Article 325 of the TFEU and is sent to the European Parliament and Council. This is the 30th such report.

4.17 As in previous years, the report summarises and evaluates measures taken by the Commission and member states to counter fraud and irregularities in relation to EU Budget funds. The report also includes both the latest information on irregularities detected by control systems and suspected fraud (with a distinction made between fraud and other irregularities), and on measures taken to deal with them. The 2018 report[19], published on 11 October 2019, covers:

- anti-fraud policies at the EU level
- detection and reporting of fraudulent irregularities that affect the EU budget

19 The 2018 Fight Against Fraud Report can be found at: https://ec.europa.eu/anti-fraud/sites/default/files/pif_report_2018_en.pdf

- measures taken by member states to counter fraud and other illegal activities which affect the EU's financial interests

4.18 The report is accompanied by five Commission Staff Working Papers: (I) Implementation of Article 325 TFEU by the member states in 2018; (ii) Statistical evaluation of irregularities reported for own resources, natural resources, cohesion policy, pre-accession assistance and direct expenditure; (iii) Follow-up recommendations to the Commission report on the protection of the EU's financial interests - Fight against Fraud 2017; (iv) Early Detection and Exclusion System (EDES) – Panel referred to in Article 108 of the Financial Regulation; and (v) Annual overview with information on the results of the Hercule III Programme in 2018.

4.19 Member states are required to report irregularities and suspicions of fraud affecting the EU's financial interests in the areas where they implement the Budget.

Irregularities reported as fraudulent

4.20 In 2018, a total of 1,152 irregularities were reported as fraudulent (suspected and established fraud), representing an increase of 0.4% compared to 2017. The estimated financial impact of irregularities reported as fraudulent was c.€1,197 million an increase of 183% on 2017[20]. Revenue had a higher number of irregularities reported as fraudulent compared to single policy areas of expenditure. However, Cohesion policy accounted for the highest value of suspected fraudulent transactions, at 81% of the total amounts involved.

Other irregularities (not reported as fraudulent)

4.21 In 2018, a total of 10,487 irregularities were reported as non-fraudulent, 26% less than in 2017. The estimated financial impact of these irregularities was c.€1.3 billion (£1.0bn).

Cases of undervaluation detected in the United Kingdom affecting TOR revenue

4.22 In November 2016, the Commission's inspection of the UK regarding TOR alleged significant weaknesses in the management and control of undervalued imports of textiles and footwear.

4.23 An OLAF investigation which concluded in 2017 alleged that appropriate measures were not taken to prevent systematically undervalued imports of textiles and footwears from China from entering the EU through the UK.

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20 2018: £1 = €1.1179055. This is the 2018 average exchange rate.

4.24 These elements led the Director-General for Budget to make a reservation in the 2016 Annual Activity report on the inaccuracy of the TOR amounts transferred to the EU budget by the UK since 2013.

4.25 The Commission started an infringement procedure in March 2018 in relation to alleged duty losses due to undervaluation fraud and the case was referred to the Court of Justice of the EU (CJEU).

4.26 The government takes these allegations extremely seriously and is strongly contesting the case. The UK submitted its Rejoinder to the Court of Justice of the EU on 21 November 2019. It adds to the UK's main Defence submitted in June 2019 and continues to make clear that the UK's response to the threat of undervaluation fraud was reasonable and did not breach its obligations under EU law. The government strongly denies that the UK caused the alleged losses to the EU budget. Even if the CJEU were to find the UK in breach of EU law, independent expert analysis demonstrates that the Commission has greatly overstated the size and severity of the alleged fraud due to methodological flaws in its analysis. The government takes customs fraud very seriously and will continue to evolve the response as new threats emerge.

4.27 The written and hearing stages of the infringement have now concluded, with the case being heard at the CJEU on 8 December 2020. The government are currently awaiting the Advocate General opinion which is due later this year with the judgment expected in 2022.

Recommendations

4.28 The report's recommendations called for all member states to:

- enhance and enforce their customs control strategies for cross-border e-commerce trade, particularly for the potential abuse of low-value consignments reliefs (LVCR) and to ensure proper TOR collection
- adopt national anti-fraud strategies, if they have not already done so

Nineteenth Report of the European Anti-Fraud Office (1 January to 31 December 2018)

4.29 The European Anti-Fraud Office (OLAF) is an administrative investigative service of the EU, with the remit of combating fraud, corruption and other illegal activities affecting the EU, including serious misconduct within the EU institutions that has financial consequences. It aims to ensure that EU taxpayers' money is spent appropriately, and that the EU is not being deprived of its due revenue.

4.30 OLAF's operational activities are independent from the European Commission and its internal (within the EU) and external (outside the EU) investigations are conducted in full independence. It investigates cases of fraud and provides assistance to the Commission and EU bodies and national authorities in their fight against fraud. It works closely with national authorities' investigation services, police, legal and administrative authorities to counter fraud. It also supports the Commission in developing anti-fraud measures.

4.31 Every year, the OLAF Director publishes a report on the activities of the Office over the previous year. The nineteenth report, issued in August 2019, gave a summary of OLAF's achievements in 2018, supported by statistics and case studies.[21]

4.32 The following statistics were reported for 2018:

- 1,211 items of information were received in 2018 from public and private sources
- 219 investigations were opened in 2018
- 256 recommendations were issued in 2018
- structural funds, centralised expenditure and EU staff accounted for the highest number of investigations
- OLAF recommended the recovery of €371 million (£285 million) as a result of investigations in 2018

21 OLAF's nineteenth activity report can be found at: https://ec.europa.eu/anti-fraud/sites/default/files/olaf_report_2018_en.pdf

4.33 In the policy field, OLAF continued to actively engage in a number of projects, including:

- improving fraud prevention and detection at EU level: the new Commission Anti-Fraud Strategy of 2019
- revision of the OLAF Regulation (EU, Euratom) No 883/2013
- the European Public Prosecutor's Office (EPPO)
- horizontal provisions on the Protection of the Financial Interests of the Union (PIF provisions) within all MFF Commission Proposals a new anti-fraud financial programme
- strengthening the EU's policy on fighting the illicit tobacco trade

4.34 In 2018, OLAF operated on an administrative budget of €59.1 million (€60.0 million).

5. Chapter 5

Government strategy on using EU funds in the UK: an update

5.1 The government is fully committed to maintaining the greatest possible transparency on the use of EU funds at a cross-government level. The 2018 annual statement, as part of the Treasury's response to recommendations from the Public Accounts Committee (PAC)[22] set out the government's strategy on using EU funds in the UK.

5.2 This year, this chapter summarises the strategy, including updates where relevant, and sets out how the government is performing in its efforts to minimise disallowance. Now the UK has left the EU, it also highlights the continuity of EU funding for the majority of programmes under the 2014-2020 Multiannual Financial Framework (MFF) under the terms of the Withdrawal Agreement.

5.3 This chapter focuses predominantly on the Common Agricultural Policy and European Structural and Investment Funds as collectively they constitute the vast majority of UK public sector receipts from the

22 PAC report on the financial management of the EU budget in 2014 can be found at: https://publications.parliament.uk/pa/cm201516/cmselect/cmpubacc/730/730.pdf; The government response can be found at: https://www.gov.uk/government/publications/treasury-minutes-november-2016

EU budget (in 2020, they accounted for 98.9 of UK public sector receipts).[23]

5.4 The UK private sector also receives a significant amount of funding through programmes directly managed by the European Commission, such as Horizon 2020. As of May, 2021[24], UK organisations have been awarded a total of €7.59 billion (£6.42 billion[25]), which accounts for 13% of the EU funding so far awarded under Horizon 2020.

5.5 In accordance with the devolution settlement, relations with the EU are the responsibility of Parliament and the government of the United Kingdom. Responsibility for implementing EU obligations relating to devolved matters lies with the devolved administrations. The proper administration of EU Funds in Northern Ireland, Scotland and Wales is a matter for the relevant devolved administration, including in relation to disallowance. This chapter and Annex D have been prepared with the main focus on English government departments and without prejudice to the devolution of these responsibilities.

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23 HMT figures, derived from Table C.3. The Home Office, for example, also manages EU funds. However, disallowance relating to those funds are not material to Home Office accounts. As set out in table D.5, for 2019-20 there were no disallowance provisions relating to 'Other' funds.

24 https://webgate.ec.europa.eu/dashboard/sense/app/a976d168-2023-41d8-acec-e77640154726/sheet/0c8af38b-b73c-4da2-ba41-73ea34ab7ac4/state/0

25 2021: £1 = €1.17358. This is the 31st March 2021 exchange rate, which provides an indicative sterling value of EU Budget receipts.

5.6 Annex D contains detailed information relating to the use of EU funds in the UK with data collated from a variety of publications, including departmental annual reports and accounts. Where relevant, key data set out in Annex D will be highlighted in this chapter, including on disallowance.

Government strategy for using EU funds

5.7 Under the Withdrawal Agreement the UK will continue to participate in programmes funded under the 2014-2020 MFF until their closure and benefit from the rights and obligations under them. As part of this continued participation, the government's overall approach to the EU budget remains to be to maximise the value for money and impact of EU spending that takes place in the UK by implementing clear strategies relating to the use of EU funds.

5.8 While the UK remained a member state, the government's approach to the EU budget continued to be to minimise UK contributions to the budget by arguing for budgetary restraint at European level.

5.9 Ultimate responsibility for implementing the EU budget lies with the European Commission. But in practice, some 80% of the EU budget is spent under what is known as 'shared management', with individual EU countries distributing funds and managing expenditure in accordance with agreements between member states and the European Commission, as well as related legislation adopted by the EU and member states. Further information on the auditing arrangements for the main shared management funds can be found in Annex D.

5.10 Reflecting the different nature of the various funds, the government has a series of strategies in place for the effective management of each of the main EU funds in the UK. Where relevant, for national allocations of EU funds, strategy documents are agreed with the Commission at the beginning of the programming period, setting out intended results and priorities to achieve maximum value for money. These are agreed in line with both EU and clearly defined domestic priorities, and typically reviewed at the midpoint of each programming period to reflect the latest outlook on economic and social positions.

Table 5.A: UK allocations for key EU funds under "shared management"

Fund	2014-20 allocation (€ billion)	2014-20 allocation (£ billion)[26]
European Agricultural Guarantee Fund (EAGF) or Pillar 1 of Common Agricultural Policy[27]	22.7	19.3
European Regional Development Fund (ERDF) + European Social Fund (ESF)[28]	10.8	9.2
European Agricultural Fund for Rural Development (EAFRD)[29]	5.2	4.4
European Maritime and Fisheries Fund (EMFF)[30]	0.2	0.2

5.11 The Common Agricultural Policy (CAP) Pillar 1, funded through the European Agricultural Guarantee Fund (EAGF), primarily involves direct payments to farmers and was the largest source of UK receipts. The CAP in England was overseen by the Department for Environment, Food and Rural Affairs (DEFRA). The Commission does not require strategic programming for EAGF, but DEFRA's

26 2021: £1 = €1.17358. This is the 31st March 2021 exchange rate, which provides an indicative sterling value of EU Budget receipts.

27 https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32012R0671&from=EN ; https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0994&from=EN ; http://data.consilium.europa.eu/doc/document/ST-14561-2014-ADD-1/en/pdf

28 European Structural and Investment Funds: UK Partnership Agreement: https://www.gov.uk/government/publications/european-structural-and-investment-funds-uk-partnership-agreement

29 http://data.consilium.europa.eu/doc/document/ST-14561-2014-ADD-1/en/pdf

30 9. https://www.gov.uk/guidance/european-maritime-and-fisheries-fund-emff-uk-managing-authority-ukma

policy approach in England for the 2014-2020 MFF was set out in a series of formal consultation responses.[31] The UK left the CAP direct payments scheme in 2020, as 2020 scheme year payments were funded from the 2021 EU budget, to which the UK did not make a contribution.

5.12 Direct payments offer poor value for money. DEFRA is committed to phasing out these payments in England over a seven-year agricultural transition period, 2021 to 2027[32]. Progressive reductions will be applied to farmers' direct payments from the 2021 scheme year. DEFRA will make the money saved from Direct Payment reductions available through schemes, grants and other types of support for farmers to manage land and their businesses more sustainably. Whilst the existing CAP schemes still operate in England, DEFRA is simplifying the rules that farmers and other beneficiaries must adhere to. This includes making simplifications to the 2020 and 2021 direct payments schemes.

5.13 European Structural and Investment Funds (ESIFs), which include the European Regional Development Fund (ERDF), the European Social Fund (ESF), the European Agricultural Fund for Rural Development (EAFRD, sometimes referred to as the second pillar of CAP) and the European

31 https://www.gov.uk/government/consultations/common-agricultural-policy-reform-implementation-in-england

32 https://www.gov.uk/government/publications/agricultural-transition-plan-2021-to-2024

Maritime and Fisheries Fund (EMFF), make up the second largest proportion of UK public sector receipts from the EU and involve investment in the real economy by supporting job creation and economic growth. The UK Partnership Agreement[33] sets out the plans and priorities for the deployment of these funds to complement EU and UK objectives on sustainable jobs and growth, and again reflects the government's overall approach set out above. The Agreement was formed by working closely with devolved administrations and with Local Enterprise Partnerships (LEPs) in England. For the 2014-20 programming period, the UK decided that the overall objectives for ESIFs would include:

- promoting sustainable and quality employment, and supporting labour mobility
- increasing the competitiveness of small and medium-sized enterprises (SMEs) and support entrepreneurism
- improving the commercialisation of research and development, including through encouraging more firms to innovate
- contributing towards improving access to, use of and quality of information and communications technology including improving superfast broadband infrastructure

33 https://www.gov.uk/government/publications/european-structural-and-investment-funds-uk-partnership-agreement

- developing infrastructure, supporting low carbon transport solutions particularly in urban areas, encouraging technological innovation and promoting energy efficiency
- improving infrastructure in less developed regions where poor connectivity contributes to market failure

5.14 Underpinning the Partnership Agreement are detailed Operational Programmes setting out the strategy and priorities for each fund in each of the constituent nations along with information about management and delivery. UK management of ESIFs has promoted value for money by setting consistent performance management standards across different programmes; establishing a strategic framework for investments; and prioritising local needs. For example, the ESF and ERDF Programmes include a requirement for applicants to demonstrate quantitative and qualitative aspects of value for money at the outline and full application stages and through ongoing contract management arrangements over the lifetime of the project.

5.15 The Department for Business, Energy and Industrial Strategy (BEIS) has overall policy responsibility for ESIFs across the UK and was responsible for negotiating the UK's Partnership Agreement with the Commission on behalf of all the UK's Managing Authorities, including the devolved administrations. Managing Authorities are responsible for negotiating and implementing individual Operational Programmes for each Fund. For England, the Managing Authorities are: Ministry of Housing, Communities and Local Government (MHCLG) for ERDF; Department for Work and Pensions (DWP) for ESF, and DEFRA for EAFRD. The Marine Management Organisation (MMO) manages the EMFF for the whole of the UK.

5.16 Annex D sets out historical information on the levels of EU expenditure in the UK between March 2011 – March 2020 and breaks down this information by Fund and, where possible, between England and the devolved administrations.

Government strategy for minimising disallowance

5.17 As part of its oversight of EU Budget spending, the Commission can impose financial corrections on member states for failing to apply EU Regulations correctly in managing and administering EU schemes. In such circumstances, the EU reduces the amount paid to the member state. These corrections are known as 'disallowance'. The UK will continue to be subject to financial corrections until all programmes for the 2014-2020 MFF have closed.

5.18 The government has taken, and will continue to take, the issue of disallowance very seriously, especially in those areas that constitute a material element of public spending in that policy area, such as CAP. As set out in the November 2016 response to the PAC, the Treasury exercises close oversight of the disallowance incurred by departments. For example, the Treasury coordinates the annual UK response to the European Court of Auditors (ECA) audit findings and, for financial errors identified by the ECA, departments are required to respond to every case and implement any required follow-up actions. Errors identified by the ECA do not necessarily lead to actual disallowance, but the ECA's findings are often followed up by the European Commission's conformity audits. The European Commission is the only actor that can apply a financial correction.

5.19 The government strategy for managing down disallowance risks consists of:

- clear central oversight and clear lines of accountability through the Treasury to departments;
- focussing efforts and investment on early identification of risks and sharing best practice where appropriate;
- while a member state, we engaged with the EU on rules governing expenditure to minimalize errors which are attributable to the complexity of the regulations governing programme participation

5.20 Robust governance and accountability arrangements are an integral part of the government's strategy for managing down the risk of financial corrections. Individual departments are accountable for developing and implementing strategies for managing expenditure risks. As part of this, departments ensure all checks on EU spending are robust, monitoring the results of audits to inform improvements. Departments and agencies managing EU funds within England have been asked to identify the main areas where they risk disallowance being imposed and implement measures to address these. Appropriate measures will vary between departments and funds, but below are examples of how DEFRA and BEIS, who have oversight of the majority of public sector EU funds in the England, are minimising the risk of disallowance.

CAP

5.21 Since the UK's exit from the EU on 31 January 2020, the UK's direct payment schemes for the 2020 scheme year onwards have not been governed by the EU's CAP legislation. This is because the CAP 2020 scheme year direct payments for farmers across the EU were funded from the 2021 EU budget, to which the UK did not contribute. The direct payments to UK farmers for the 2020 scheme year were instead funded by the exchequer.

5.22 DEFRA implemented its Disallowance Strategy in 2014 to manage the ongoing risk of disallowance. The strategy was reviewed in 2016 and again following the EU Exit referendum to ensure that the strategy still delivers value for money in light of EU Exit. DEFRA continue to review the strategy to make sure action is taken to minimise our exposure to disallowance as we exit from the CAP.

5.23 Historically, no member state has achieved zero disallowance under the CAP regime, illustrating the complexity of the schemes and the challenges and costs of complying with them. Investment in the land register has removed the previous main causes of disallowance under earlier CAP scheme audits, and there is now no single overriding cause of disallowance. In recent audits, DEFRA have had more success in being able to demonstrate that control deficiencies affect limited and known amounts of expenditure.

5.24 The Rural Payments Agency (RPA) England works to minimise disallowance through a range of approaches to audit findings, including:

- improving inspections and administrative controls;
- providing evidence of any compensatory controls;
- undertaking targeted data analysis;
- undertaking retrospective checks to demonstrate controls;

- where there is a weakness in controls, working to ‘ring-fence’ audit findings to specific relevant areas to demonstrate a more proportionate risk to EU Funds;
- managing the financial impact where a policy decision has an inherent disallowance risk

5.25 The effectiveness of this approach is exemplified by the 2019 Area Aids Audit, which resulted in a correction of £19.3 million (final sterling value to be confirmed later this year). This is less than half of the £42.5 million forecast and significantly less than the £402 million disallowance that would have been applied, had the Defra Disallowance Strategy not been adopted.

5.26 There are outstanding decisions on audit enquiries concerning expenditure under the first pillar of CAP. Future EU disallowance will only concern expenditure under the second Pillar resulting from current and further audits for programmes funded under the 2014-2020 MFF until their closure.

5.27 Continued EU engagement is necessary:

- The CAP is governed by complex rules, which drive up the risk and incidence of disallowance. DEFRA challenges the Commission’s proposals for disallowance where it believes that the proposals are disproportionate relative to the risk to the fund, often resulting in lower disallowance being applied.

- DEFRA also engages with the devolved administrations, exchanging information about the scope and outcome of EU audits in order to improve assessment of disallowance risks and will continue to monitor the outcome of relevant audit activity in EU Member States.

5.28 Progress in implementing DEFRA's disallowance strategy is overseen by the Department's Disallowance Steering Group, which meets bi-monthly. It is important to note that the impacts of mitigating actions can take time to crystallise.

ESIFs

5.29 BEIS works with the Managing Authorities (including MHCLG, DWP and DEFRA) and the devolved administrations to ensure that the ESIFs are managed appropriately. Managing Authorities must demonstrate that they comply with certain criteria set out in the ESIF's regulations.

5.30 BEIS and Managing Authorities have put in place an early warning system to identify potential disallowance quickly using the Partnership Agreement Programme Board. The Board continues to meet regularly to share expertise and best practice between the Managing Authorities and BEIS and to identify lessons learnt. Managing Authorities also provide financial updates on their ESIF programmes, raise issues and seek clarifications. In addition, Managing Authorities are drawing on the experiences from previous programming periods to counteract the risk of disallowance. These include a strengthening of administrative and on-the-spot control checks and checking all expenditure prior to paying out to beneficiaries or reclaiming it from the Commission.

5.31 Projects are risk assessed and scored as part of approval and in most Managing Authorities a control plan is put in place, with higher risk scores leading to more intensive scrutiny. Verification checks of expenditure vary between the Managing Authorities, but typically include desk checks, site visits and expenditure checks by the Certifying Authority – which is responsible for guaranteeing the accuracy and honesty of statements of expenditure and requests for payments before they are sent to the European Commission.

5.32 Across all funds, a range of networks exist to share learning and best practice both between UK authorities and with other member states. The UK continued to participate in these while an EU member state. Following the exit from the EU, the UK no longer attends formal EU meetings and expert groups on shared management programmes. However, where required UK Managing Authorities, Devolved Administrations and EU officials remain in contact to discuss financial issues related to the management of ESIF programmes until their closure. For example, in 2020, the UK made positive use of the flexibilities related to the use of ESIFs under the European Commission's Coronavirus Response Investment Initiative (CRII). UK Managing Authorities identified over £400m of re-purposed funds from the 2014-2020 ESIF programmes which have been committed to CRII projects across the UK to address the economic and health care impacts of Coronavirus COVID-19. This is not additional funding, but the repurposing of uncommitted funds or reallocated funds from existing commitments within the 2014-2020 ESIF programmes. The CRII projects will be managed within current ESIF programmes until December 2023, after which they will be closed.

5.33 In addition to domestic efforts, the UK continued to engage with the EU until exit. This included working on the rules governing EU expenditure and continuing to push for simplified rules across all areas of EU expenditure. Many errors in EU spending are due to the complexities of the regulations governing different programmes, therefore simplifying the rules will reduce the number of errors and reduce the disallowance incurred.

Information on disallowance

5.34 As set out in previous statements, government departments publish information about possible disallowance in their departmental annual accounts and reports. A disallowance provision is recognised in departmental accounts where there is a past event (for example an ineligible payment or a failure to comply with the regulations) which is likely to lead to the EU disallowing expenditure and not reimbursing the UK. The Treasury monitors disallowance provisions.

5.35 Annex D sets out historical information on disallowance and future provisions for them. As noted above, under the Withdrawal Agreement the UK will continue to participate in programmes funded under the 2014-2020 MFF until their closure, and as part of this will continue to have robust audit arrangements and provide updates regularly published by departments. In subsequent annual statements the government will update on performance against the strategies above for programmes we continue to participate in under the 2014-2020 MFF. Further information on reporting for EU programmes that we will participate in under the Trade and Cooperation agreement, or other financing agreements, is set out at Annex F.

5.36 Tables D.5 and D.6 in Annex D set out data from the 2018-19 and 2019-20 departmental accounts respectively. These include:

- provisions for future corrections added to departmental accounts over the course of the relevant financial year; provisions ‘released’ by departments during the year, which is the value of provisions no longer expected to materialise into actual disallowance;

- and provisions ‘utilised’ in year, which is the value of provisions that are expected to materialise within 12 months (they are no longer a future long-term liability but are expected to be imposed by the European Commission).

5.37 The updated data set out in Table D.5 is discussed in more detail in the next section of this chapter.

5.38 Whilst information on disallowance provisions can, to some extent, indicate levels of likely disallowance, it is important to note that this information cannot be used to identify trends or measure the success of related strategies because:

- disallowance provisions added to Statements of Financial Position in any given year can relate to activity that has taken place in a number of previous years;
- disallowance can be challenged by departments and are sometimes successfully overturned;
- as set out earlier in this chapter, disallowance is often illustrative of the complexity of the regulations governing EU funds rather than any misuse of funds, and disallowance may increase temporarily following the introduction of new scheme rules;

- figures may not be directly comparable across funds, due to the different ways in which funds work and different levels of complexity of the various programmes;
- there may be a lag between action being taken by a department to reduce disallowance and the effect being observable

Update on performance and minimising disallowance

5.39 At European level, UK engagement with the EU institutions and member states has led to a range of UK proposals on simplification and harmonisation being included in the Commission's proposed changes to EU regulations. These changes will continue to support the effective use of EU funds in the UK while the UK continues to participate in programmes funded under the 2014-2020 MFF until their closure. At the domestic level, progress in using EU funds in this programming period is being made and initial updates on how departments are minimising disallowance is available.

5.40 DEFRA delivered CAP Pillar 1 since the beginning of the 2014-2020 programming period in line with the key principles of supporting a competitive farming sector, simplifying the schemes where possible and minimising implementation and disallowance costs. For example, in implementing the EU greening requirements, which set out environmental and ecological conditions for the use of funds, DEFRA took advantage of the discretion member states had to implement EU rules flexibly, and provided a package of options which gave farmers a choice over how they complied with the rules. Under the terms of the Withdrawal Agreement the UK funded 2020 scheme year Basic Payment Scheme (BPS) payments. This is because 2020 scheme year payments provided to Member States were funded from the 2021 EU budget, to which the UK did not contribute to. This gave the UK some limited freedom to make changes to the 2020 scheme year BPS, such as simplifying penalties for smaller overclaims of land in England, and not be subject to disallowance for these domestically funded BPS payments. From the 2021 scheme year, following the end of the transition period with the EU, the UK has further opportunity to make changes to the existing schemes. In England, this further flexibility has been used to remove the ineffective greening rules and make other simplifications to BPS.

5.41 In relation to disallowance, DEFRA's strategy is proving to be a success in reducing penalties on CAP expenditure for the 2014-20 period. In several recent audits the initial disallowance amount proposed has reduced significantly solely due to this strategy. For example, in addition to the significant recent reduction noted in paragraph 5.25 above, in an audit of Area Aids 2016 a €410 million initial proposal was reduced to €28.9 million.

5.42 As demonstrated by the data in Table D.5, the majority of provisions in 2019-20 continue to be related to agricultural policy funding. They have increase significantly from 2018-19 (set out in Table D.6) due to the audits covering 3 years of expenditure for the BPS which is the largest element of funding. The difference in size of provisions for agricultural funding compared to other EU schemes is largely due to the size of the fund. Based on recent data, the new provisions are in respect of BPS 2017-2019 scheme years and Cross Compliance 2017-2019 scheme years. However, financial provisions for EU audits on agricultural funding routinely fluctuate throughout the audit process before final confirmation, and as such final figures are subject to change and will reduce significantly. The current CAP disallowance strategy reflects the latest intelligence from these processes and will continue to be updated.

5.43 During calendar year ending 2020, verification activity continued to identify irregular expenditure, across a number of issues, to give a level of assurance and compliance by the grant recipients before inclusion of claims within a payment application. Cross-cutting themes and document retention guidance was issued in February 2018 and all verification managers ensure project managers understand these Regulatory requirements. In terms of disallowance, the ESIFs strategy is working effectively at this stage. Table D.5 shows that in 2019-20 there remain some financial correction provisions relating to the European Social Fund managing exchange rate risk, but these continue to be relatively small.

EU funding under the Withdrawal Agreement

5.44 To reiterate, under the Withdrawal Agreement, the UK will continue to participate in programmes funded under the 2014-2020 MFF until their closure. This means that the vast majority of programmes will continue to receive EU funding across the programme's lifetime. In many cases, funding will continue after 2020 until 2023 when the programmes will close. UK organisations can continue to apply for EU funding under the current MFF, with the exception of the CAP Pillar 1 Direct Payments scheme which the UK left in 2020.

5.45 The government previously guaranteed EU funding to provide certainty for UK beneficiaries. With the Withdrawal Agreement in force the guarantee was no longer required. In the very limited number of cases where continued participation by the UK is not possible for security related reasons, these projects will be eligible to enter a continuation process. The government's commitment to fund the tail of CAP

Pillar 2 financial liabilities that exceed the 2014-2020 MFF also still stands.

A. Annex A

Glossary

Agreed Upon Procedures (AUPs)

A.1 An engagement to perform agreed upon procedures (AUPs) may involve the auditor performing certain procedures concerning individual items of financial data. The objective of an agreed upon procedures engagement is for the auditor to carry out procedures of an audit nature to which the auditor and the entity (and any appropriate third parties) have agreed, and report on factual findings. Users of the report assess for themselves the procedures and findings reported by the auditor and draw their own conclusions from the auditor's work.

Commitment and payment appropriations

A.2 The EU budget distinguishes between appropriations for commitments and appropriations for payments. Commitment appropriations are the total cost of legal obligations that can be entered into during the current year, for activities that, in turn, will lead to payments in current and future years. Payment appropriations are the amounts of money that are available to be spent during the year, arising from commitments in the Budgets for the current or preceding years. Unused payment appropriations may, in some circumstances, be carried forward into the following year.

Discharge procedure

A.3 The ECA's annual report is subject to consideration by the budgetary authority (Council and European Parliament) under the "discharge procedure" set out in Article 319 of the Treaty on the functioning of the EU[34]. In particular, it considers how the budget for the year in question was implemented. The European Parliament, acting on a recommendation from the Council, considers whether to grant the Commission a discharge in respect of the budget in question, thus bringing the budgetary process for that year to a formal close. The Commission is obliged under Article 319 (3) of the Treaty on the functioning of the EU to take "all appropriate steps" to act on comments made by the European Parliament and by the Council during the discharge process. It must also report back to the budgetary authority on follow-up actions taken in response to Parliament and Council's recommendations.

Error in EU Budget expenditure

A.4 The European Court of Auditors (ECA), established to audit the EU's finances, provide annual statements on the legality and regularity of the

34 Consolidated Version of the Treaty on the Functioning of the European Union: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:12012E/TXT&from=en

transactions underlying EU spending. A summary of the statement for Budget year 2018 is set out in chapter 4. As part of their statement, the ECA estimates the level of error present in EU Budget expenditure, due to it not being used in accordance with EU rules. Whilst the ECA calculate error rates for the EU Budget as a whole, they are clear that they only sample a limited number of transactions in each member state and the "relative frequency of error in samples drawn in different member states cannot be a guide to the relative level of error in different member states". The errors identified by the ECA do not necessary lead to actual disallowance. More information on disallowance in the UK is contained in chapter 5.

European Structural and investment funds

A.5 European Structural and Investment Funds (ESIFs), often referred to as Structural Funds, are intended to resolve structural economic and social problems. For the 2014-20 programming period, the Common Provisions Regulation sets out the guiding principles for administering the funds. At present, these funds are:

- the European Regional Development Fund (ERDF), which promotes economic and social cohesion within the EU through the reduction of imbalances between regions or social groups

- the European Social Fund (ESF), which promotes the EU's employment objectives by providing financial assistance for vocational training, retraining and job creation schemes
- the European Agricultural Fund for Rural Development (EAFRD), which contributes to the structural reform of the agriculture sector and to the development of rural areas
- the European Maritime and Fisheries Fund (EMFF), the specific fund for the structural reform of the fisheries sector
- the Cohesion Fund (CF), which supports member states with GDP that is less than 90% of the European average, financing environmental and trans-European transport projects

Financing Share

A.6 The UK's "financing share" of the EU budget is calculated annually and determines the amount of UK contributions to the EU budget (taking into account the rebate) relative to all Member State contributions to the EU budget.

Flexibility Instrument

A.7 The Flexibility Instrument was established under paragraph 24 of the 1999 Inter-institutional

Agreement[35] and amended as part of the Mid-Term Review of the MFF[36]. This allows for expenditure in any given Budget year of up to €600 million (2011 prices) above the MFF ceilings established for one or more Budget headings. The amount available is also increased annually by the amount of EU Solidarity Fund and EU Globalisation Adjustment Fund allocations which lapse (or are unused) in the previous year. Any portion of the Flexibility Instrument unused at the end of one year may be carried over for up to three subsequent years. The Flexibility Instrument is intended 'to allow the financing, for a given financial year, of clearly identified expenditure which could not be financed within the limits of the ceilings available for one or more other headings'[37]. It may only be used after all possibilities for reallocating existing appropriations have been exhausted. Both arms of the budgetary authority must agree to a mobilisation of the Flexibility Instrument following a proposal from the Commission.

35 Inter-institutional Agreement of 6 May 1999 between the European Parliament, the Council and the Commission on budgetary discipline and improvement of the budgetary procedure: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:31999Y0618(02)

36 Amending regulation: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R1123&from=EN

37 Regulation laying down the multiannual financial framework for the years 2014-2020: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32013R1311

Fraud and irregularity

A.8 **Fraud** covers intentional acts or omissions, in respect of both expenditure and revenue, which involved the use or presentation of false, incorrect or incomplete statements or documents, or specific non-disclosure of information, or misapplication of funds or benefits.

A.9 **Irregularity** (as defined by Council Regulation 2988/95) covers 'any infringement of a provision of Community law' caused by an act or omission which leads to reduction in EU revenue, or loss or misspending of EU funds. Irregularities are distinct from fraud in that they are financial errors as opposed to intentional, criminal misuse of funds. For example, a genuine payment made after the closing date for claims represents an irregularity; but import of goods under false papers is fraud.

Inter Institutional Agreement (IIA)

A.10 The IIA is a politically and legally binding agreement that clarifies the EU's budgetary procedure. The Council and the European Parliament have joint responsibility for deciding the EU Budget on the basis of proposals from the Commission. The IIA sets out the way in which the three institutions will exercise their responsibilities and their respect for the revenue ceilings that are laid down in the Own Resources Decision. In particular, it provides for the annual EU Budget to be set in the context of an MFF.

Own Resources

A.11 The Own Resources Decision lays down three sources of EU revenue, or "Own Resource": customs duties, including those on agricultural products, in respect of trade with non-member countries and levies on sugar production within the Union. These are collectively known as "Traditional Own Resources" (TOR);

- customs duties, including those on agricultural products, in respect of trade with non-member countries and levies on sugar production within the Union. These are collectively known as "Traditional Own Resources" (TOR)
- contributions based on VAT: Essentially, the VAT resource is the amount yielded by applying a notional rate of 1% to a hypothetical harmonised VAT base, assuming an identical range of goods and services in each member state. The VAT base is calculated on the basis of a notional harmonised rate and reflects finally taxed expenditure across the EU. The base is capped at 50% of the member state's GNI. A call-up rate is applied to produce a member states' VAT-based contribution. This is currently 0.3%, except otherwise noted in the Own Resources Decision

- GNI-based contributions: the amount due is calculated by taking the same proportion of each member state's GNI. As EU budgets must balance, revenue must equal expenditure. The GNI-based resource is the Budget-balancing item; it covers the difference between total expenditure in the Budget and the revenue from the other resources, subject to the overall Own Resources ceiling

Sterling figures

A.12 The figures referred to in pounds sterling for 2013-19 in this document are based on actual Sterling cash receipts, or payments where these took place and are known. Elsewhere, the appropriate annual average sterling/euro exchange rate has been used to convert Euro figures into Sterling[38]. The 2020 Euro figures have been converted into Sterling using the Sterling/Euro exchange rate on 31st December 2019, namely £1 = €1.17536 (regulations state that VAT-based and GNI-based payments will be made using the exchange rate on the last working day of the preceding year). However, there may be some exceptions, for example where figures have previously been published at a different exchange rate, but these are noted where necessary.

38 The annual average rate for 2012 is £1 = €1.233211; the annual average rate for 2013 is £1 = €1.177910; the annual average rate for 2014 is £1 = €1.240977; the annual average rate for 2015 is £1 = €1.377415; the annual average rate for 2016 is £1 = €1.220286; the annual average rate for 2017 is £1 = €1.1413; the annual average rate for 2018 is £1 = €1.30319; the annual average rate for 2019 is £1 = €1.13925.

UK-EU Trade and Cooperation Agreement

A.13 The UK-EU Trade and Cooperation Agreement (TCA) was announced on 24 December 2020, a week before the end of the transition period. It was signed on 30 December 2020 and ratified by the European Parliament on 28 April 2021. Within the scope of this statement the TCA governs continued UK participation in some EU programmes: Horizon Europe (Research), Euratom Research and Training, ITER fusion and Copernicus (satellite system).

UK rebate

A.14 The UK's GNI-based contributions are abated (reduced) according to a formula set out in the Own Resources Decision. Broadly, this is equal to 66% of the difference between what the UK contributes to the EU Budget and its receipts from the EU Budget, subject to the following points:

- the rebate applies only in respect of spending within the EU
- the UK's contribution is calculated as if the Budget were only financed by TOR and VAT-based contributions
- the rebate is deducted from the UK's GNI-based contribution a year in arrears, e.g. the rebate in 2015 relates to UK payments and receipts in 2014

- since 2011 the UK's contributions to non-agricultural expenditure in member states that have acceded to the EU in or after 2004 are not abated. This reflects the agreement by the UK government in 2005 to "disapply" the UK rebate on non-agricultural expenditure in new member states

A.15 The formula for the calculation of the rebate is set out in the Own Resources Decision, and in a Working Methods Paper first published in 1988 and revised in 1994, 2000, 2007 and 2014.

A.16 The Commission is directly and solely responsible for calculating the UK's rebate. It calculates the rebate on the basis of a forecast contributions to the EU Budget and the UK's receipts from it. This is subsequently corrected in light of outturn figures.

A.17 Corrections may be made for up to three years after the year in respect of which the rebate relates, with a final calculation then being made in the fourth year, e.g. a final calculation of the rebate in respect of 2016 will take place in 2020.

A.18 The effect of the rebate is to reduce the amount of the UK's monthly GNI-based payments to the EU Budget. It does not involve any transfer of money from the Commission or other member states to the Exchequer.

Withdrawal Agreement

A.19 The Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community, (the Withdrawal Agreement) was received Royal Assent on 23 January 2020 and was signed on 24 January 2020. The European Union (Withdrawal Agreement) Act 2020 has given effect to the financial provisions within the Withdrawal Agreement in domestic law.

B. Annex B

Technical annex

Explanation of the difference between the government's cash flow outturn for the UK's net contribution for 2019 and the figures in the European Commission's EU Budget 2019 Financial Report

B.1 As set out in Chapter 3, paragraph 3.8, there is a difference between the UK government's figures for the cash flow outturn for the UK's net contribution for 2019 and the figures in the European Commission's EU Budget 2019 Financial Report. An explanation for this difference is set out in Table B.1, Table B.2 and paragraphs B.3 to B.4.

B.2 When converted with the average exchange rate for 2019 of £1= €1.13925, the figures on cash flow outturn for the UK's net contribution for 2019 in the European Commission's EU Budget 2019 Financial Report break down as set out in Table B.1.

Table B.1: Cash flow outturn for the UK's net contribution for 2019 in the European Commission's EU Budget 2019 Financial Report

	(€ million)	(£ million)
UK gross contribution before rebate	22,248	19,528
UK rebate	-5,101	-4,477
UK receipts	-7,636	-6,702
UK net contribution	9,511	8,349

Source: European Commission's EU Budget 2019 Financial Report, HM Treasury calculations

B.3 The government's figure for the UK's net contribution in 2019 is £8,349 million.

B.4 A number of factors contribute to the difference between the two net contribution figures. The main causes for the difference are as follows:

- the UK figure includes only transactions between the EU Budget and the UK public sector, whereas the European Commission's figure includes receipts paid directly to the UK private sector. It is estimated that this accounted for around £1,681 million of the difference in 2019
- the UK's outturn figure is based on cash flow within the calendar year, whereas the European Commission figures attempt to match transactions to a particular EU Budget. When reconciling there may be other factors such as the exchange rate that can lead to differences between the outturns

- in 2018 Amending Budget 6/2018 was adopted on the 12th of December. This meant that associated changes were not implemented until 2019, the result of which is that the government's figures are some £651 million higher than if the Amending Budget changes had been implemented in 2018.

B.5 These factors are set out in Table B2.

Table B.2: Reconciliation of the UK government's cash flow outturn figures for the UK's net contribution for 2019 with the figures in the European Commission's EU Budget 2019 Financial Report

	(£ million)
UK government outturn for 2019	9,408
Private sector receipts	-1,681
Late implementation, in January 2019, of Amending Budget 6/2018	651
Late implementation in January 2020	-
UK cash flow figure adjusted to reflect main differences compared to European Commission's figure	8,379
European Commission figure for 2019 outturn	8,349
Net difference due to other factors (e.g. exchange rate)	30

Source: HM Treasury calculations and 2019 EU Budget Financial Report, European Commission

C. Annex C

Tables

C.1 This annex includes tables that supplement data presented in the main text.

C.2 Table C.1 covers expenditure on the EU Budget commitments and payments by Heading in years 2012-2019 in euro figures.

C.3 Table C.2 covers expenditure on the EU Budget commitments and payments by Heading in years 2012-2019 in sterling figures.

C.4 Table C.3 covers UK contributions to, rebate and public sector receipts from the EU Budget in years 2012 - 2019.

Table C.1: Expenditure on the EU Budget Commitments and Payments by Heading in years 2013-2020 (€ million)

Appropriations	**Commitments**							
	2013	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
1 Smart and Inclusive Growth	70,749	63,986	77,955	69,841	75,399	77,532	80,627	85,931
1a Competitiveness for Growth and Jobs	*15,641*	*16,484*	*17,552*	*19,010*	*21,312*	*22,000*	*23,435*	***25,286***
1b Economic, social and territorial cohesion	*55,108*	*47,502*	*60,403*	*50,831*	*54,087*	*55,532*	*57,192*	***58,646***
2 Sustainable Growth: natural resources	60,102	59,191	63,877	62,470	58,569	59,239	59,642	59,907
3 Security and Citizenship	2,197	2,172	2,522	4,292	4,284	3,493	3,787	7,152
4 Global Europe	9,315	8,423	8,711	9,167	10,437	10,069	11,319	10,992
5 Administration	8,431	8,405	8,660	8,951	9,395	9,666	9,943	10,271
TOTAL	152,048	142,690	162,273	155,277	159,831	160,696	166,189	172,253
Appropriations	**Payments**							
	2013	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
1 Smart and Inclusive Growth	69,127	65,863	66,854	59,291	49,393	66,663	67,557	77,454
1a Competitiveness for Growth and Jobs	*12,612*	*11,857*	*15,729*	*17,402*	*19,321*	*20,095*	*20,522*	***22,308***
1b Economic, social and territorial cohesion	*56,473*	*54,006*	*51,125*	*41,888*	*30,073*	*46,527*	*47,035*	***55,146***
2 Sustainable Growth: natural resources	58,036	55,959	55,979	54,972	54,121	56,041	57,400	57,904
3 Security and Citizenship	1,669	1,660	1,927	3,022	3,224	2,981	3,527	6,369
4 Global Europe	6,743	6,925	7,478	10,156	9,056	8,906	9,358	9,112
5 Administration	8,429	8,406	8,659	8,951	9,395	9,666	9,945	10,274
TOTAL	144,451	139,034	141,280	136,642	126,771	144,768	148,492	161,113

Notes:

1. 2013-20 include all agreed Amending Budgets.
2. Column totals do not necessarily equal the sum of individual items due to rounding errors and spending not attributable to any heading.

Source:

Figures for 2013 to 2017 are taken from the European Commission's Reports on budgetary and financial management.

Figures for 2018 and 202 are taken from the final agreed Amending Budget in each year.

European Commission Budget website: https://ec.europa.eu/info/strategy/eu-budget/documents/annual-budget_en

Table C.2: Expenditure on the EU Budget Commitments and Payments by Heading in years 2013-2020 (£ million)

Appropriations								**Commitments**
	2013	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
1 Smart and Inclusive Growth	60,063	51,561	56,595	57,233	66,064	68,789	72,124	**71,408**
1a Competitiveness for Growth and Jobs	*13,279*	*13,283*	*12,743*	*15,578*	*18,674*	*19,519*	*20,964*	***21,512***
1b Economic, social and territorial cohesion	*46,785*	*38,278*	*43,852*	*41,655*	*47,390*	*49,270*	*51,160*	***49,896***
2 Sustainable Growth: natural resources	51,024	47,697	46,375	51,193	51,318	52,558	53,352	**50,969**
3 Security and Citizenship	1,865	1,750	1,831	3,517	3,754	3,099	3,387	**6,085**
4 Global Europe	7,908	6,787	6,324	7,512	9,145	8,933	10,125	**9,352**
5 Administration	7,158	7,158	6,773	6,773	8,231	8,576	8,894	**8,739**
TOTAL	129,083	114,982	117,810	127,246	140,043	142,575	148,661	**146,553**
Appropriations								**Payments**
	2013	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
1 Smart and Inclusive Growth	58,686	53,074	48,536	48,588	43,278	59,145	60,432	**65,898**
1a Competitiveness for Growth and Jobs	*10,707*	*9,555*	*11,419*	*14,261*	*16,929*	*17,829*	*18,357*	***18,980***
1b Economic, social and territorial cohesion	*47,943*	*43,519*	*37,117*	*34,326*	*26,350*	*41,280*	*42,075*	***46,918***
2 Sustainable Growth: natural resources	49,270	45,093	40,641	45,048	47,420	49,721	51,346	**49,265**
3 Security and Citizenship	1,442	1,338	1,399	2,476	2,825	2,645	3,155	**5,418**
4 Global Europe	5,725	5,580	5,429	8,323	7,935	7,902	8,371	**7,753**
5 Administration	7,156	6,774	6,286	7,335	8,231	8,576	8,896	**8,741**
TOTAL	122,633	112,036	102,569	111,975	111,076	128,442	132,831	**137,075**

Notes:

1. 2010-16 includes all agreed Amending Budgets.
2. Column totals do not necessarily equal the sum of individual items due to rounding errors and spending not attributable to any heading.

Source: Sterling figures are derived from the corresponding euro amounts in Table C.1 converted at the appropriate exchange rate (see Glossary).

Table C.3: United Kingdom contributions to, rebate, and public sector receipts from the EU Budget 2012-2019

	EUR Millions								GBP Millions							
Gross Contributions	2013	2014	2015	2016	2017	2018	2019	**2020**	2013	2014	2015	2016	2017	2018	2019	**2020**
Sugar levies	11	2	10	9	10	-3	0	**0**	9	2	7	7	9	-3	0	**0**
Customs Duties	2,557	2,775	3,192	2,997	3,610	2,943	3,031	**2,764**	2,171	2,236	2,318	2,456	3,163	2,611	2,711	**2,352**
VAT–based contributions	2,761	2,963	3,665	3,266	3,470	3,465	3,316	**3,317**	2,344	2,388	2,661	2,677	3,040	3,074	2,966	**2,822**
GNI-based contributions	15,899	15,539	19,288	14,468	13,872	16,080	15,700	**18,897**	13,497	12,521	14,003	11,856	12,154	14,267	14,044	**16,077**
VAT & GNI adjustments	134	2,024	786	0	295	-2,824	-869	**1,164**	114	1,631	571	0	258	-2,505	-777	**990**
United Kingdom rebate	-4,328	-5,481	-6,768	-4,732	-6,429	-4,787	-5,048	**-6,113**	-3,674	-4,416	-4,914	-3,878	-5,633	-4,247	-4,516	**-5,201**
Total Contributions	17,034	17,822	20,174	16,008	14,828	14,876	16,132	**20,032**	14,461	14,362	14,646	13,118	12,993	13,198	14,430	**17,043**
PUBLIC SECTOR RECEIPTS																
EAGF	3,236	3,395	3,251	2,766	3,103	3,085	3,143	**3,219**	2,747	2,736	2,361	2,267	2,719	2,737	2,812	**2,739**
EAFRD	729	529	637	488	722	567	761	**782**	619	426	462	400	633	503	681	**665**
European Regional Development Fund	350	1,311	625	439	327	765	609	**768**	297	1,057	454	360	286	678	545	**654**
European Social Fund	290	331	780	375	162	333	1,009	**413**	246	266	566	308	142	295	903	**352**
Other Receipts	102	122	55	195	347	74	91	**60**	86	98	40	160	304	65	82	**51**
Total Receipts	4,707	5,688	5,348	4,263	4,661	4,823	5,614	**5,243**	3,996	4,583	3,883	3,493	4,084	4,279	5,022	**4,461**
Net Public Sector Contributions	12,327	12,135	14,825	11,745	10,168	10,053	10,518	**14,789**	10,465	9,779	10,763	9,625	8,909	8,919	9,408	**12,583**

1. For all years, the amounts for the UK's gross contribution in this table reflect payments made during the calendar year, not payments to particular EU Budgets. They differ from the figures for gross contributions in Table 2 in that these figures, drawn from European Commission documents, relate to payments to particular EU Budgets.
2. Prior to 2010, Sugar Levies row also includes figures for duties on agricultural products.
3. Euro figures in this table have been converted from sterling using the appropriate exchange rate (see glossary).
4. The figures for 2015 are based on the Office of Budget Responsibility Forecast and HM Treasury calculation. Those for earlier years are outturn.
5. The VAT and GNI adjustment figure shown in 2014 includes £1.7 billion for which the UK has made cash payments in two instalments in 2015, but the full amount is accrued to 2014, as set out in paragraph 4.138 in the Office for Budget Responsibility's December 2014 Economic and Fiscal Outlook.
6. Because of rounding, the column totals do not necessarily equal the sum of the individual items.
7. Additional to regular contributions, total contributions include payments of late interest to the EU.

D. Annex D

Report on the use of EU funds in the UK

Background

D.1 This annex is linked to, and has cross references with, Chapter 5 on the government strategy for using EU funds in the UK. As part of ongoing work to improve the accountability for, and transparency of, EU funds, this annex is produced to collate and present data from a variety of publications on the use of EU funds in the UK.

D.2 The publication of this report strengthens Parliamentary scrutiny of the financial relationship between the EU and the UK government. It is compiled by working with Paying Agencies and Managing Authorities. The Report draws on well-established data collection and assurance systems and processes.

D.3 The government is committed to maintaining the greatest possible transparency on the use of EU funds at an aggregated level by publishing information such as this until the data is no longer relevant due to the exhaustion of EU funds

Responsibilities of the UK Parliament and Devolved Administrations

D.4 As highlighted in Chapter 5, in accordance with the devolution settlement, relations with the EU are the responsibility of Parliament and the government of the United Kingdom, as the former member state. Responsibility for implementing EU obligations relating to devolved matters lies with the devolved administrations. The proper administration of EU Funds in Northern Ireland, Scotland and Wales is a matter for the relevant devolved administration. This report is prepared without prejudice to the devolution of responsibilities.

D.5 The Treasury has assumed responsibility for developing the format of this report and for collating the financial data provided by Paying Agencies and Managing Authorities which it includes. Managing Authorities are the bodies which have responsibility for managing the payment of EU programme funds to final beneficiaries in the UK.

D.6 Paying agencies and Managing Authorities, however, remain accountable for the propriety of the reported spending, which is publicly disclosed in their annual report and accounts and is subject to external audit. This report therefore brings together financial information relating to the use of

EU funds by the UK but does not replace individual accountabilities. The Comptroller and Auditor General (C&AG) of the National Audit Office has not been invited to audit this report although most of the individual annual report and accounts, from which the source data is collated, are audited by the C&AG (with the remainder of annual reports and accounts audited by the Auditor General for Wales, the Comptroller and Auditer General for Nothern Ireland and Auditor General for Scotland).

Boundary of the report

D.7 The report shows expenditure on co-managed EU schemes in the UK and the corresponding income due from the EU. The main schemes for which the EU and UK share management responsibility are the disbursement of Common Agricultural Policy Funds and the European Structural and Investment Funds, where the UK pays beneficiaries on behalf of the EU.

D.8 The report excludes:

- amounts received from the EU where UK central government is the beneficiary
- amounts in respect of commercial contracts awarded to UK central government bodies by the EU

- financial support for twinning projects where EU funding is transferred to other member states or to mandated bodies for their part in the project.[39] Those transactions are not reported as income and expenditure of the relevant Managing Authority
- the purchase of intervention stocks with UK funds which are accounted for in the financial statements of the Department for Environment, Food and Rural Affairs (DEFRA)[40]

Management of EU funded schemes

D.9 The Treaty establishing the EU provides the basic framework for its Budget. The Budget includes a number of separate funds, including the European Agricultural Guarantee Fund (EAGF), the European Regional Development Fund (ERDF), the European Social Fund (ESF), the European Agricultural Fund for Rural Development (EAFRD and sometimes referred to as the second pillar of Common Agricultural Policy) and the European Maritime and Fisheries Fund (EMFF).

39 Twinning projects are EU funded projects that support the capacity building in new member states or the Candidate Countries. They are delivered by the public sector, usually by central government. These are funded through pre-accession funds.

40 Intervention stocks are stocks held by paying agencies in the EU as a result of intervention buying of commodities subject to market support. Intervention stocks may be released onto the internal markets if internal prices exceed intervention prices; otherwise, they may be sold on the world market.

D.10 These schemes are overseen by the European Commission. Responsibility for financial reporting to the Commission falls to national authorities who are responsible for the co-management of schemes with Managing Authorities.

D.11 The Commission can impose disallowance on Managing Authorities for failing to correctly apply EU Regulations in managing and administering EU schemes. In such circumstances the EU reduces the amount paid to the UK.

(a) Agricultural Policy Funds

D.12 The Single Payment Scheme (SPS) was the main agricultural subsidy scheme in the EU, funded by the EAGF. It was replaced by the Basic Payment Scheme in January 2015.

D.13 Under EU Regulation 907/2014, each paying agency must have an internal audit service independent of the other departments that reports directly to the Head of the paying agency. Paying agencies are the bodies of a member state responsible for disseminating payments of EU funds to approved programmes, keeping accurate information on these payments and guaranteeing compliance with EU legislation. The internal audit services are required to verify that the procedures adopted by the agency are adequate to ensure compliance with Union rules and that accounts are accurate, complete and timely.

D.14 The Certification Body for the agricultural funds are appointed external auditors that report on: whether the annual accounts of the paying agencies are in all material respects true, complete and accurate; that internal control procedures have operated satisfactorily; the legality and regularity of expenditure and; the assertions made in the annual Management Declarations made by the Heads of paying agencies. The Certification Body reports have confirmed that internal audit units in all the UK paying agencies operate to a high standard, although they have in turn highlighted issues that require appropriate remedial action to avoid disallowance.

(b) European Structural and Investment Funds

D.15 The European Structural and Investment Funds are the financial tools set up to implement cohesion policy in the EU, and include ERDF, ESF, EAFRD and EMFF. For more details on these programmes please refer to the Glossary of this document.

D.16 The Managing Authorities are responsible for the control of European Structural and Investment Fund expenditure. Working alongside each fund's Managing Authority, the fund's Certifying Authority ensures that all systems are subject to regular examination by the Audit Authority. The Audit Authority results strengthen procedures during the implementation of programmes and provide assurance as to the accuracy, completeness and regularity of expenditure, certified to the European Commission.

D.17 The Managing Authorities are responsible for the control of European Structural and Investment Fund expenditure. Working alongside each fund's Managing Authority, the fund's Certifying Authority ensures that all systems are subject to regular examination by the Audit Authority. The Audit Authority results strengthen procedures during the implementation of programmes and provide assurance as to the accuracy, completeness and regularity of expenditure, certified to the European Commission.

Timing of the expenditure and the related EU funding

D.18 Managing Authorities are required to account for expenditure on EU-funded schemes and the related funding from the EU on an accruals basis under International Financial Reporting Standards (IFRS) as applied to the public sector context by the Government Financial Reporting Manual (FReM). By contrast, the public sector receipts in Table C.3 are reported on a cash basis.

D.19 There is normally a time lag between payment to beneficiaries and settlement of claims by the

EU. The UK Exchequer therefore bears the cost of the programme until EU funding is received. Expenditure is recognised as it is incurred, with a matching receivable (debtor) from the EU. The receivable is extinguished when the EU approves the subsequent claim and the release of funds to the UK.

D.20 The final settlement of claims by the EU may give rise to adjustments following the closure process or disallowance (see paragraphs D.31-D.32 below). The European Commission may make such adjustments several years after funds have been paid out by Managing Authorities to recipients. The Expenditure Statement below also includes provisions for possible future adjustments. A provision is made where it is probable that the EU will disallow expenditure and not reimburse the UK (see paragraph D.31 below).

Management of EU funded schemes

Expenditure on EU funded schemes

D.21 This section of the document covers the expenditure on EU funded schemes between 2011-12 and 2019-20.

D.22 The Expenditure Statement (Table D.1) shows the EU funded element of amounts paid out by UK central government bodies on projects supported wholly or partially by the EU on which the UK anticipates EU funding at the point the payment is made.

D.23 Gross expenditure on EU supported projects is recognised in the period in which it becomes payable by UK central government to the recipient under the rules of the relevant scheme. The amount shown in the Expenditure Statement represents the amount paid and payable in Sterling during the period to beneficiaries.

D.24 Net expenditure represents the amount receivable from the EU in respect of amounts paid or payable by the UK on EU supported projects, after taking account of provisions for disallowance, foreign exchange gains or losses and withdrawals from claims.

D.25 The Statement of Assets and Liabilities (Table D.2) shows those assets and liabilities that stem from cash flows, where, for example, the UK has paid a claim from a beneficiary and is awaiting reimbursement from the EU. The disallowance provision relates to amounts paid out by the UK for which it believes it probable that the EU will apply financial corrections and not fully reimburse the UK.

D.26 The Expenditure Statement (Table D.1) shows gross expenditure on EU-supported schemes from 2011-12 to 2019-20. After allowing for foreign exchange variations and adjustments to claims, the amount reimbursable by the EU (i.e. net expenditure) was £5.43 billion in 2018 -19 and £3.72 billion in 2019-20, the balance being met by the UK Exchequer. Underlying this was a reduction in gross expenditure, an increase in provisions created in year, largely due to agricultural funding provisions (Table D.5), and an increase in foreign exchange variations. Prior years have been restated where necessary to amend previously published figures in order to reflect the correction of errors, new information that has arisen or a change in accounting policy. A breakdown of expenditure by scheme is provided in Tables D.3 to D.4. This table shows that the decrease in net expenditure between 18-19 and 19-20 is due to European Social Fund gross expenditure and European Regional Development Fund gross expenditure, which decreased across the years. While gross expenditure on Agricultural Funding did not decrease significantly the disallowance provisions made in 2019-20 reduced the net position. A breakdown of provisions by scheme is provided in Tables D.5 and D.6 with further explanation at D.31-33.

Accounting policies

Basis of preparation

D.27 This report has been prepared by collating the relevant transactions and balances as recorded by the Managing Authorities in their financial statements. Their financial statements have been prepared in accordance with the FReM.

Foreign currency translation

D.28 The European Commission makes payments in Euros, with the Managing Authority recognising the receivable in Sterling in line with the requirements of International Accounting Standard (IAS) 21 The Effects of Changes in Foreign Exchange Rates.

The effects of changes in Foreign Exchange Rates

D.29 Foreign exchange rate gains and losses are realised where there are variations in exchange rates between payments incurred and reimbursements. For example, for ERDF, ESF and EMFF, there is often an exchange rate difference due to the lag between the date when EU funding is paid out by the Managing Authority and the date when this payment is subsequently checked and registered by the Certifying Authority, on which basis the EU reimburses the expenditure incurred. Such gains and losses are recognised in the Expenditure

Statement (Table D.1). Unrealised gains and losses arising from the revaluation of assets and liabilities at the exchange rate current at the Statement of Financial Position date, also reported in the Expenditure Statement, are reported in the accounts of Managing Authorities within the Statement of Changes in Taxpayers' Equity. Any hedging mechanisms used to mitigate the impact of foreign exchange losses are not included in this report, as they do not impact on the amounts paid out on EU projects or the funding provided by the EU.

Disallowance provision and contingent liabilities

D.30 Probable disallowance arising from financial corrections are recognised in accordance with the requirements of IAS 37 Provisions, Contingent Liabilities and Contingent Assets. A provision is recognised where there is a past event – for example an ineligible payment or a failure to comply with the regulations governing a scheme – which will probably lead to the EU disallowing expenditure and not reimbursing the UK. Managing Authorities are responsible for estimating the value of any provisions required.

Table D.1: Expenditure Statement for the years ended 31 March 2012 to 31 March 2020 (prior years restated)

									£ thousand
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Gross expenditure on EU supported projects	4,773,977	4,216,794	4,345,271	4,254,226	3,361,171	3,774,481	3,812,404	5,286,320	4,429,695
Provisions created in year	(92,647)	(34,850)	(1,832)	(21,459)	(32,568)	(120)	0	(9,488)	(647,477)
Provisions released in year	22,817	10,495	60,452	11,770	335	1,198	8,692	169,701	14,889
Realised forex gain/(loss)	(23,617)	114,930	2,019	(30,005)	(12,012)	2,491	(2,271)	6,633	(82,511)
Unrealised forex gain/(loss)	51,182	(102,488)	(13,637)	51,733	(163,305)	(4,158)	16,470	(14,629)	9,906
Withdrawn from EU claim	(18,063)	(35,841)	(8,036)	1,171	2,858	(26,450)	(1,870)	(2,404)	(1,177)
Net expenditure reimbursable by the EU	4,713,649	4,169,040	4,384,237	4,267,436	3,156,479	3,747,442	3,833,425	5,436,133	3,723,325

* 2019-20 balances include the latest available information. Some Managing Authority returns may be based on unaudited financial statements

Table D.2: Statement of Assets and Liabilities as at 31 March 2012 to 31 March 2020 (prior years restated)

									£ thousand
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Assets									
Advances to beneficiaries	25,594	17,340	26,143	24,788	26,640	42,262	148,886	53,479	122,877
EU funds receivable	1,763,336	1,763,235	2,314,084	1,622,625	2,146,918	1,219,556	1,492,592	1,754,606	1,262,028
Other assets	254,299	207,990	258,436	281,893	484,815	408,996	450,327	199,554	897,611
	2,043,229	1,988,565	2,598,663	1,929,306	2,658,373	1,670,814	2,091,805	2,007,639	2,282,516
Liabilities									
EU funds paid on account	(1,860,340)	(997,802)	(655,634)	(530,013)	438,265	(379,520)	(667,295)	(241,104)	(482,958)
Amounts payable to beneficiaries	(183,401)	(186,053)	(148,459)	(73,928)	(328,505)	(424,239)	(577,389)	(558,005)	(390,197)
Repayable to EU	(2,697)	(238,694)	(543,684)	(737,127)	(685,287)	(645,931)	(557,983)	(486,299)	(306,623)
Provision for disallowance	(212,390)	(214,681)	(100,154)	(5,585)	(34,180)	(245,558)	(184,080)	(24,264)	(648,476)
Other liabilities	(66,734)	285	517	517	(2,885)	(151)	(12,951)	(503,259)	(612,655)
	(2,325,562)	(1,636,945)	(1,447,414)	(1,346,136)	(612,592)	(1,695,399)	(1,999,698)	(1,812,931)	(2,440,909)
Net Assets / (Liabilities)	(282,333)	351,620	1,151,249	583,170	2,045,781	(24,585)	92,107	194,708	(158,393)

*2019-20 balances include the latest available information. Some Managing Authority returns may be based on unaudited financial statements

The 2018-19 figures have been corrected from last year’s publication.

Table 3.D: Analysis of Net Expenditure by EU Scheme 2018-19

										£ thousand
	Agricultural Funding		European Social Fund		European Regional Development Fund		Other		Total	
	England	DAs	England	DAs	England	DAs	England	DAs	England	DAs
Gross expenditure in the United Kingdom	2,441,829	1,130,073	799,573	103,341	574,283	195,003	24,580	17,638	3,840,265	1,446,055
Total disallowance provided for	(9,488)	0	0	0	0	0	0	0	(9,488)	0
Total disallowance released	169,581	120	0	0	0	0	0	0	169,581	120
Total foreign exchange gains/(losses)	1,161	(109)	(12,693)	4,110	(4,685)	(379)	3,752	847	(12,465)	4,469
Total withdrawn from EU claim	0	0	0	(444)	(1,528)	(432)	0	0	(1,528)	(876)
Net expenditure reimbursable by EU	2,603,083	1,130,084	786,880	107,007	568,070	194,192	28,332	18,485	3,986,365	1,449,768
Total Net expenditure reimbursable by EU		3,733,167		893,887		762,262		46,817		5,436,133

Table 4.D: Analysis of Net Expenditure by EU Scheme 2019-20*

										£ thousand
	Agricultural Funding		European Social Fund		European Regional Development Fund		Other		Total	
	England	DAs	England	DAs	England	DAs	England	DAs	England	DAs
Gross expenditure in the United Kingdom	2,330,816	1,067,341	414,675	94,559	307,101	165,870	22,695	26,638	3,075,287	1,354,408
Total disallowance provided for	(647,477)	0	0	0	0	0	0	0	(647,477)	0
Total disallowance released	14,889	0	0	0	0	0	0	0	14,889	0
Total foreign exchange gains/(losses)	(69,721)	0	10,510	(77)	(5,592)	(600)	(6,784)	(341)	(71,587)	(1,018)
Total withdrawn from EU claim	0	0	0	(87)	(911)	(179)	0	0	(911)	(266)
Net expenditure reimbursable by EU	1,628,507	1,067,341	425,185	94,395	300,598	165,091	15,911	26,297	2,370,201	1,353,124
Total Net expenditure reimbursable by EU		2,695,848		519,580		465,689		42,208		3,723,325

*2019-20 balances include the latest available information. Some Managing Authority returns may be based on unaudited financial statements.

Provisions of future financial corrections (disallowances)

D.31 As previously stated in Chapter 5, a disallowance is a financial correction imposed by the European Commission on member states for failing to correctly apply EU Regulations in managing and administering EU schemes. In such circumstances the EU reduces the amount paid to the UK.

D.32 The European Commission may identify erroneous payments or deficiencies in the administration of schemes, and consequently can disallow expenditure. In the case of perceived systematic deficiencies, the European Commission can impose flat-rate disallowance at the rate of 2%, 3%, 5%, 7% or 10% (or higher in some circumstances) of annual expenditure, depending on the severity of the failings. The EU will not reimburse the UK for the expenditure incurred. The costs then fall on the Exchequer, unless the amount can be recovered from the beneficiary. The ultimate financial impact on the UK taxpayer will, however, be less than this, due to the operation of the rebate system. For more details on the rebate system please see the Glossary of this document.

D.33 As set out in Chapter 5, table D.4 and D.5 show that the majority of provisions in 2019-20 continue to be related to agricultural funding; this is largely due to the size of the fund and the complexity of the regulations. There was an increase in provisions in 2019-20 due to audits covering 3 years of expenditure for the Basic Payment Scheme, which is the largest element of funding. Further information on this is set out in Chapter 5 (see paragraphs 5.40 – 5.42). The current CAP disallowance strategy reflects the latest intelligence from these processes and will continue to be updated. In 2019-20, there also remain some provisions relating to the European Social Fund managing exchange rate risk, but these continue to be relatively small (see table D.5). DEFRA continues to review the strategy to make sure action is taken to minimise our exposure to disallowance as we exit from the CAP.

Table 5.D: Provision in England and the DAs for future financial corrections 2019-2020

										£ thousand
	Agricultural Funding		European Social Fund		European Regional Development Fund		Other		Total	
	England[41]	DAs[42]	England[43]	DAs[44]	England[45]	DAs[46]	England	DAs	England	DAs
As at 1 April 2019	(23,264)	0	0	(1,000)	0	0	0	0	(23,264)	(1,000)
Created during the year	(647,477)	0	0	0	0	0	0	0	(647,477)	0
Released in year	14,889	0	0	0	0	0	0	0	14,889	0
Utilised	8,376	0	0	0	0	0	0	0	8,376	0
As at 31 March 2020	(647,476)	0	0	(1,000)	0	0	0	0	(647,476)	(1,000)
Total as at 31 March 2020		(647,476)		(1,000)		0		0		(648,476)

Notes: In England: agricultural funding is primarily the responsibility of the Department for Environment, Food & Rural Affairs (the European Maritime and Fisheries Fund, included in agricultural funding figures, is the responsibility of the Marine Management Organisation, an executive non-departmental public body sponsored by DEFRA); the European Social Fund is the responsibility of the Department for Work and Pensions; the European Regional Development Fund is the responsibility of Department for Communities and Local Government. 'Other' contains small funds, such as the Asylum, Migration, and Integration Fund (AMIF), which is the responsibility of the Home Office. As at 31 March 2020, there were no provisions relating to 'Other' funds). The DAs are responsible for implementing EU obligations relating to devolved matters.

41 https://www.gov.uk/government/publications/defras-annual-report-and-accounts-2019-to-2020 (this includes the European Maritime and Fisheries Fund)

42 https://www.gov.scot/publications/scottish-government-consolidated-accounts-2019-2020/

43 https://www.gov.uk/government/publications/dwp-annual-report-and-accounts-2019-to-2020

44 https://www.gov.scot/publications/scottish-government-consolidated-accounts-2019-2020/

45 https://www.gov.uk/government/publications/mhclg-annual-report-and-accounts-2019-to-2020

46 https://www.gov.scot/publications/scottish-government-consolidated-accounts-2019-2020/

Table 6.D: Provision in England the DAs for future financial corrections 2018-2019

										£ thousand
	Agricultural Funding		European Social Fund		European Regional Development Fund		Other		Total	
	England[47]	DAs[48]	England[49]	DAs[50]	England[51]	DAs[52]	England	DAs	England	DAs
As at 1 April 2018	(184,158)	(120)	0	(1,000)	0	0	0	0	(184,158)	(1,120)
Created during the year	(9,488)	0	0	0	0	0	0	0	(9,488)	0
Released in year	169,581	120	0	0	0	0	0	0	169,581	120
Utilised	801	0	0	0	0	0	0	0	801	0
As at 31 March 2019	(23,264)	0	0	(1,000)	0	0	0	0	(23,264)	(1,000)
Total as at 31 March 2019		(23,264)		(1,000)		0		0		(24,264)

Notes: In England: agricultural funding is primarily the responsibility of the Department for Environment, Food & Rural Affairs (the European Maritime and Fisheries Fund, included in agricultural funding figures, is the responsibility of the Marine Management Organisation, an executive non-departmental public body sponsored by DEFRA); the European Social Fund is the responsibility of the Department for Work and Pensions; the European Regional Development Fund is the responsibility of Department for Communities and Local Government. 'Other' contains small funds, such as the Asylum, Migration, and Integration Fund (AMIF), which is the responsibility of the Home Office. As at 31 March 2019, there were no provisions relating to 'Other' funds). The DAs are responsible for implementing EU obligations relating to devolved matters.

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47 https://www.gov.uk/government/publications/defras-annual-report-and-accounts-2018-to-2019 (this includes the European Maritime and Fisheries Fund)

48 https://www.gov.scot/publications/scottish-government-consolidated-accounts-year-ended-31-march-2019/

49 https://www.gov.uk/government/publications/dwp-annual-report-and-accounts-2018-to-2019

50 https://www.gov.scot/publications/scottish-government-consolidated-accounts-year-ended-31-march-2019/

51 https://www.gov.uk/government/publications/mhclg-annual-report-and-accounts-2018-to-2019

52 https://www.gov.scot/publications/scottish-government-consolidated-accounts-year-ended-31-march-2019/

E. Annex E

Impact of EU Withdrawal

E.1 OverviewThe UK left the EU on 31 January 2020 following the Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community, (the Withdrawal Agreement) signed on 24 January.[53]

E.2 The Withdrawal Agreement was followed by a transition period in which the UK was no longer a member of the EU but remained a member of the single market and customs union. During that time, it continued to be subject to EU rules and obligations to contribute to the EU Budget. The transition period ended on 31 December 2020, which is the EU's financial year-end date and the reporting date used for reporting on the UK's outstanding net liabilities.

E.3 The Withdrawal Agreement sets out the financial settlement that was reached on the UK's rights and obligations as a departing member state. The settlement is based on three agreed principles that ensure a fair deal for UK taxpayers:

- the UK will not finance any commitments that it would not have funded if it had remained a Member

53 https://www.gov.uk/government/publications/new-withdrawal-agreement-and-political-declaration

State, and will receive a share of any financial benefits that would have fallen to it had it remained a Member State

- the Withdrawal Agreement establishes the UK's share of EU obligations in the settlement. For 2020, the share will be based on the current methodology for determining the UK's annual EU budget contributions. For payments after the end of the Transition period, it will be based on the UK's average share of contributions to the EU during the current Multiannual Financial Framework. In other words, the UK's share will be the average of its share of the EU budget (taking into account the rebate) over 2014-20
- the UK will not be required to incur expenditure earlier than would have been the case had it remained a Member State, although the Withdrawal Agreement allows for exceptions to be made in a few specific cases where it might be in both sides' interests to settle costs early. This is particularly relevant for pensions, where costs will decline steadily over a long-term period

E.4 This annex includes a summary of the first payment request of UK net liabilities made by the EU under the Withdrawal Agreement, with an explanation of the UK's strategy for assurance of the financial provisions of the Withdrawal Agreement. It summarises the technical engagement between the

UK and the EU on implementation of the financial provisions, and the formal governance of that relationship.

E.5 It also sets out the government's revised point estimate of the financial settlement based upon the UK's departure from the EU on 31 January 2020, which remains within the range of HMT's original estimate, adjusted for the extension in the negotiation period for the UK's exit from the EU under Article 50 of the Treaty on European Union. It provides a summary of the financial settlement and its estimated cost, alongside costs outside the financial settlement that are set out in the Withdrawal Agreement. The financial settlement has three main components:

- first, the UK continued to participate in EU annual budgets during 2020. This means that the UK continued to make its contribution and get receipts from EU budget programmes under the normal rules
- second, the UK will then pay its share of the EU's outstanding commitments at the end of 2020 (the so-called RAL) and again will benefit from some of these commitments
- third, the UK will pay a share of the EU's liabilities as at the end of 2020, and any materialising contingent liabilities, and in return will benefit from a share of relevant EU assets

E.6 It then explains how different approaches can be taken to the presenting the 'cost' of the settlement, depending on the accounting or reporting framework used and the assumptions and methods used to estimate values. The approach will be different in specific government publications (e.g. HM Treasury Accounts; Whole of Government Accounts or the Office of Budget Responsibility's Economic and Financial Outlook).

E.7 The financial settlement addressed mutual obligations that arose primarily as a consequence of the UK's participation in the EU budget, and commitments related to the UK's broader membership of the EU. It did not cover the costs of facilitating withdrawal or new administrative arrangements that might have resulted from the UK's exit. There was also no obligation in the financial settlement to pay for the relocation of EU bodies previously located in the UK.

E.8 The financial settlement did not cover costs that might be associated with the UK's future relationship with the EU. These were subject to negotiations on our future relationship with the EU and are covered by the EU-UK Trade and Cooperation Agreement, signed by the parties on 30 December 2020. This agreement is considered separately in Annex F.

The European Union (Withdrawal Agreement) Act 2020

E.9 The European Union (Withdrawal Agreement) Act 2020 (WAA) implemented the Withdrawal Agreement into domestic law. It received Royal Assent on 23 January 2020.

E.10 Section 20 of the WAA on financial provisions allows the government to meet the financial obligations set out in the Withdrawal Agreement. The legislative mechanism in the Act is a standing service provision until 31 March 2021. The Act does not grant payment authority relating to any future agreements between the UK and EU.[54]

Participation in the European Union annual budget in 2020

E.11 Under the financial settlement, the UK contributed to the EU's budget for the whole of 2020 during the Transition period implemented after the UK left the EU. The UK benefited from the implementation of the budget as if it had remained a Member State over this period. The UK will continue to draw advantages from the normal management of projects and programmes funded through the 2014-2020 Multiannual Financial Framework until

54 European Union (Withdrawal Agreement) Act 2020 Section 20(2) The standing services provision only applies to sums required to be paid in respect of the traditional own resources of the EU after 31 March 2021.

their closure, whether they are managed by the UK government (such as the European Regional Development Fund) or directly allocated to beneficiaries from EU institutions (such as Horizon 2020).

E.12 The Withdrawal Agreement guarantees that any amendments made to the Multiannual Financial Framework after withdrawal do not apply to the UK, insofar as they impact upon the UK's financial contributions and that the UK is not obliged to contribute to any additional funding beyond what is set out in the Withdrawal Agreement. The UK is also unaffected by any changes made after withdrawal to the core rules on budget revenue in the Own Resources Decision which impact on the UK's financial contributions. This is to protect the UK from any such changes that are made now that we have left. One technical issue has arisen during the period covered by this statement relating to amendments to the Multiannual Financial Framework and this is discussed from paragraph E.45.

E.13 UK contributions to the EU Budget over 2020 were paid from the Consolidated Fund, in the same way as the UK's contribution while we were a Member State. Similarly, individual departments that administer receipts and do not act purely as an agent of the EU, will continue to account for these receipts in their resource accounts.

EU outstanding budget commitments

E.14 A normal consequence of the EU's multiannual approach to spending is that many payments are made some years after a commitment is made. This is because the EU budget finances projects that run over multiple years, and which are subject to financial controls and programme conditionality. As a result, at any given time there is a stock of outstanding commitments that are yet to be paid – referred to as reste à liquider or RAL. The Withdrawal Agreement sets out that the UK will pay its share of these commitments as at 31 December 2020 as these commitments fall due. The UK will also benefit from some of these commitments, since it will benefit from EU programmes committed to under the Multiannual Financial Framework 2014-20 until the closure of those programmes.

Assets and liabilities

E.15 The UK will pay its share of the EU's liabilities as at 31 December 2020 and will benefit from a share of EU assets in a number of ways. In some cases, for example property and buildings, the asset reduces or removes a liability that might otherwise have fallen to the UK. In others, for example investment assets associated with EU guarantees, the UK will get a share of the profits and original investment as they mature.

E.16 The most significant residual liabilities are in relation to the pensions and other employee benefits of the members and staff of the European institutions. The UK will contribute towards those pension rights accrued on or before 31 December 2020. The UK will pay its share of these pension rights as the costs fall due to the EU, unless the UK decides to settle this early.

E.17 The financial settlement also includes a number of contingent liabilities, most of which were reported to Parliament as remote contingent liabilities when the UK was a Member State. These fell outside the scope of international accounting standards (IAS 37 on Provisions, Contingent Liabilities and Contingent Assets) because the possibility of an outflow of resources is remote.

E.18 In most cases the contingent liabilities that remain under the financial settlement will be limited to those that the EU has taken on up to the date of withdrawal. The exception will be costs associated with legal cases related to the budget and linked policies and programmes, which will be limited to cases where the facts relate to the period of the UK's participation in the EU budget (before the end of 2020).

E.19 Many of the contingent liabilities relate to guarantees on financial operations managed by the EU and its implementing partners. Under the financial settlement the UK obtains a share of the associated guarantee funds the EU accumulated to meet potential calls on these underlying operations. To the extent the UK's share of these guarantee funds is not drawn upon to meet calls on the financial operations the UK will receive a positive return from these instruments.

E.20 In addition, the UK's EIB paid-in capital of €3.5 billion will be returned over 12 years, starting in the year of withdrawal. This will be made in 11 yearly instalments of €300 million and the final reimbursement will cover the balance of €195,903,950. The UK received the first instalment of €300 million from the EIB on 15 October 2020, in line with the provisions of the Withdrawal Agreement.[55] The UK will maintain a two-part contingent liability in respect of the stock of outstanding EIB operations at the point of the UK's withdrawal, which will decrease in line with the stock. Under the terms of the EU Withdrawal Act the return of the UK's EIB paid-in capital remained an asset of the Consolidated Fund unless the asset

55 The date of the initial instalment of the return of EIB paid-in capital set out in Article 150(4) was amended by Article (1)(6)(a)(i) of Decision 1/2020 of the Withdrawal Agreement Joint Committee from 15 December 2019 to 15 October 2020 in order to account for the revised date upon which the UK left the EU. Further details are provided under the description of the Withdrawal Agreement governance from Paragraph E.41

was transferred to HM Treasury. The first instalment of reimbursement has been transferred to HM Treasury and are disclosed in HMT's departmental resource accounts for 2020-2021.

Payments made under the Withdrawal Agreement

E.21 UK contributions to the EU Budget over 2020 were based on established processes and a consistent control environment. The Withdrawal Agreement provides for continued UK attendance at relevant meetings in respect to the implementation of the Own Resources system (the system of rules for calculating Member State contributions to the EU Budget). The institutions of the Union continue to be audited by the European Court of Auditors (ECA) in their implementation of the EU Budget, as they did when the UK was a member state.

E.22 The final payment in respect of the UK's period of membership of the EU, rather than under the Withdrawal Agreement was made in February 2021. Payments after this point have been made in accordance with the specific methodology set out in the Withdrawal Agreement and new assurance processes have been developed accordingly. These are summarised from paragraph E.28

E.23 The EU will issue two invoices per year, in April and September. The UK will pay the net liability or settlement at the end of June and October, respectively. The April invoice includes a schedule for equal payments in the following 4 months and the September invoice is followed by 8 further monthly instalments.[56]

E.24 The EU issued the first request for payment of the UK's outstanding net liabilities under the Withdrawal Agreement on 16 April 2021, in line with the requirements of Article 148.

E.25 The April 2021 invoice provides a single net liability for the UK of €3,763,622,581.98 (£3,206,418,258.72)[57] payable in four equal instalments from 30 June to 30 September 2021. HM Treasury scrutinised the April invoice to confirm that it is in line with the interpretation of the Withdrawal Agreement agreed with the European Commission and its entrusted entities during technical work on the implementation of the financial provisions and is content with its accuracy, validity and completeness.

E.26 HM Treasury carried out a specific series of analytical checks on receipt of the April invoice and before payment which are detailed below. These include analysis of consistency with:

56 Article 148

57 All liabilities under the Withdrawal Agreement are settled in Euros and the Sterling value provided here is based on the conversion rate applied by the European Central Bank on the first working day of April 2021

- European Commission financial reporting delivered during 2020 (detailed at E.33)
- European Commission financial reporting delivered in March 2021 (detailed at E.36)
- agreements made during technical engagement and formal governance (detailed at E.41 and Box E.3)
- HM Treasury internal modelling and estimates for the financial settlement (detailed at E.53)

E.27 The initial payment was made by the UK at the end of June. HM Treasury will report in detail on the payments made under the WA in 2021 in the next statement, relating to 2021.

Assurance on the financial settlement

E.28 Article 134 of the Withdrawal Agreement gives the UK the right to appoint entities to carry out audit activities in respect of the implementation of the financial provisions, supported by appropriate administrative arrangements. The information obtained by the UK and the audit work undertaken will provide assurance to the government on the implementation of the financial settlement and provide confidence to Parliament that what is paid and received is in accordance with the Agreement.

E.29 We have worked with the European Commission and its implementing partners to ensure their systems and controls over financial reporting are suitable for the specific requirements of the Withdrawal Agreement. We recognise that it's in the interest of both parties (and member states) that the UK pays the right amount of liabilities, and receives its share of receipts, due under the Withdrawal Agreement. We have agreed technical interpretations, consistent with the principles underpinning the Withdrawal Agreement. These are based on methodologies which are fair to both parties and which result in net liabilities being met at the correct time (including receipts due to the UK). Our formal and technical engagement with the European Commission is set out from paragraph E.42. Our approach to obtaining assurance over the financial settlement is summarised in Box E.1:

Box E.1: Overview of the UK's assurance of the financial settlement

Assurance of the financial settlement has been based on a risk-based approach to financial reporting:

- mapping key reporting risks to the UK; understanding where reliance can be placed on assurance processes that are unchanged from our period of EU membership, and agreeing additional arrangements to obtain comfort over risks that were not mitigated by those controls
- a tailored approach to obtain comfort over the payments and reimbursements as they arise on an article-by-article basis in order to assess the completeness and accuracy of future assets, liabilities, payments and receipts
- reliance, where possible, on the European Commission's (and other entrusted entities') independently audited financial statements and other independent data testing in order to minimise the repetition of audit work (recognising that the absence of an established reporting framework to form the basis of an assurance opinion made the appointment of a single UK auditor of the financial settlement impossible)

- the ability to trace net liabilities from the European Commission's audited accounts (and those of its implementing partners) to both the more detailed Withdrawal Agreement reporting obligations and to the April invoice
- where the existing reporting and assurance does not address specific reporting risks to the UK resulting from the Withdrawal Agreement, HMT has requested specific additional procedures are performed, including through the use of Agreed Upon Procedure (AUP) reports on the data underlying the European Commission's formal reporting to the UK. These AUP reports provide independent factual findings of tests agreed with the UK to support our assurance objectives. A definition of AUPs is provided in the Glossary at A.1.

Reliance on the EC's annual accounts

E.30 The EC's annual accounts for the years ending 31 December 2020 onwards contain additional disclosures related to UK Withdrawal from the EU.[58] Obligations in respect of the following Withdrawal Agreement provisions are covered:

- Article 140 - Outstanding commitments (the RAL)

58 https://ec.europa.eu/info/publications/annual-accounts-2020_en

- Article 142 - Union liabilities at end 2020 (Commission pension schemes)
- Article 136 - Provisions applicable in relation to own resources
- Article 141 - Fines
- Article 143 - Contingent financial liabilities: loans for financial assistance (EFSI, EFSD & ELM);
- Article 144 - Financial instruments
- Article 145 – Assets of the European Coal and Steel Community, in liquidation
- Article 146 - Investment in the European Investment Fund (EIF)
- Article 147 – Contingent liabilities related to legal cases

E.31 The European Commission prepares the European Commission annual accounts on the basis of European Union Accounting Rules, which are based on the International Public Sector Accounting Standards (IPSAS). These are based on public sector interpretations of the International Financial Reporting Standards (IFRS). The EU annual accounts are audited by the European Court of Auditors (ECA). The ECA conducts its audit in compliance with the International Standards on Auditing (ISAs) and is independent of the European Commission, in accordance with the International

Ethics Standards Board for Accountants (IESBA) Code of Ethics for Professional Accountants. The ECA audit opinion is discussed in greater detail in Chapter 4.

E.32 The ECA is free to decide what it will audit, how it will do this, and how and when to present its findings. As a result, the ECA reports two annual opinions:

- **'True and fair'** - whether the European Commission accounts, are properly prepared in accordance with international public sector accounting standards and present a materially correct view of financial results for the year and assets and liabilities at the end of the year.
- **'Legal and regular'** - whether the European Commission accounts are made up of transactions that comply with applicable EU rules, regulations and contractual obligations.

European Commission financial reporting delivered during 2020

E.33 The UK is liable under the Withdrawal Agreement for its share of the contingent financial liabilities of the Union arising from the financial operations (budgetary guarantees and financial assistance programmes) decided upon or approved by 31 January 2020, the date that the UK left the EU.

Conversely, the UK is due its share of contributions to the guarantee funds that support these financial operations. Further detail on these liabilities is provided at paragraph E.65.

E.34 The Withdrawal Agreement required the EU to provide by 31 July 2020 an initial report on the scope and value of these contingent financial liabilities on the day that the UK left the EU and these reports were delivered as required.[59] The reports enabled the UK to assess the accuracy and completeness of the relevant liabilities based on:

- access to the reporting templates which were submitted by each of the Commission's implementing partners and used to compile the reports
- validation of a complete list of relevant financial operations
- third party reports of factual findings from a list of agreed test objectives (AUPs)

E.35 The reports delivered in 2020 were the precursor to annual reporting from 31 March each year on the value of the net contingent financial liabilities at the end of the preceding calendar year. Procedures were included in the AUPs performed to test whether the amount of financial liabilities relating to

59 Article 144(1) of the Withdrawal Agreement, as amended by Articles 1(3) and 1(4) of Decision 1/2020 of the Withdrawal Agreement Joint Committee.

operations at exit day were reported correctly as the basis for future reporting on the value of outstanding liabilities each year.

European Commission financial reporting due annually in March from 2021

E.36 As is the case with contingent financial liabilities, the Withdrawal Agreement specifies that the European Commission must provide detailed financial reporting in March of each year on other net liabilities recorded at the end of the preceding year. We have worked with the European Commission to ensure that this reporting supports the UK's assurance objectives.

E.37 We received the March 2021 reports in line with the requirements of the Withdrawal Agreement. They reflect the UK's position at the end of the transition period on 31 December 2020 and form a basis for the net liabilities that the UK began to settle in June. The reports delivered in 2021 are summarised in Box E.2, and will be supplemented in future years to cover net liabilities which are only due from 2022, including pensions.

Box E.2: Overview of the March reporting deliverables

The European Commission provided the UK with a reporting package and supporting annexes comprising the following:

- financing share of the United Kingdom (2014-2020) which is a calculation input into each component of the net liability under the Withdrawal Agreement[60]
- outstanding commitments at 31 December 2020 for which the UK is liable which relates to the RAL liabilities resulting from our membership of the EU[61]
- contingent financial liabilities arising from loans for financial assistance and budgetary guarantees (European Fund for Strategic Investments, European Fund for Sustainable
- financial operations under financial instruments financed by the programmes of the MFF 2014-2020 (or earlier financial perspective)[62]

60 Article 139 WA. The UK's 'financing share' of the EU budget is calculated annually and determines the amount of UK contributions to the EU Budget (taking into account the rebate) relative to all Member State contributions to the EU Budget. Its calculation and effect on the UK's share of net liabilities is discussed from Paragraph E.85.

61 Article 140 WA

62 Article 144 WA

- amounts to be paid in relation to contingent liabilities arising from legal cases to which the EU was a party until the end of the transition period.[63]

E.38 We have taken a tailored approach to obtaining comfort over the payments and reimbursements as they arise for each article to assess the completeness and accuracy of future assets, liabilities, payments and receipts. This has involved validating the data in the key reporting products from the Commission against:

- the internal modelling developed by HMT to estimate the liabilities arising from the Withdrawal Agreement (discussed from paragraph E.53)
- publicly available data and historic data held by the UK from our period of membership
- prior years' audited accounts of the Commission and its delivery partners
- reporting templates used by the European Commission to compile the formal reports due under the Withdrawal Agreement and, where available, audit opinions relating to the Commission's implementing partners

63 Article 147 WA

- the Commission's draft accounts, which include new specific UK Withdrawal disclosures that will be subject to an audit opinion[64]
- other underlying data provided by the Commission as evidence for the basis of its calculation methodology

E.39 This programme of work has resulted in more than 40 individual checks on the reported net liabilities and the new disclosures in the EU's annual accounts (discussed from paragraph E.30). The principal focus of HMT's verification work has been to check that the:

- UK's financing share has been calculated and applied consistently according to the methodology prescribed in Article 139 of the Withdrawal Agreement
- RAL liabilities which form the largest element of the settlement are in line with agreed interpretations, conform to our expectations based on published information and the internal modelling presented in this statement, and match a new specific, disclosure made in the EU annual accounts that is within the scope of the ECA audit opinion

64 Any reconciliation required between draft and audited accounts will be resolved using the adjustment process discussed from Paragraph E.49

- Financial instruments, Budgetary Guarantees and Financial Assistance Programmes are consistent with previously reported balances and other sources of information over which we have third party reports against test objectives that we have specified or influenced (including testing for completeness against the list of operations reported by the European Commission in July 2020 described at paragraph E.34)

E.40 Collectively, these reports allow us to cross-reference with both the European Commission annual accounts disclosures, the first April invoice and underlying supporting data provided to us. We have engaged with the European Commission to probe and challenge the integrity of the reporting, pursue queries and test the data provided. In undertaking this work we have adopted a risk-based approach to assessment of these liabilities, considering both qualitative and quantitative criteria.

Technical engagement and formal governance

E.41 On 30 March 2020 the Withdrawal Agreement Joint Committee (WAJC) tasked the Specialised Committee on Financial Provisions (SCFP) to start work related to implementing the financial provisions in Part V of the Withdrawal Agreement. The SCFP is co-chaired by HMT officials and by representatives of the European Commission. This formal governance has supported our assurance objectives and provides a prescribed route for escalation of any areas of disagreement to the WAJC.

E.42 The first meeting of the SCFP was held in May 2020 and the parties reaffirmed their commitment to complying with their legal obligations under the Withdrawal Agreement. There was agreement to continue work on the information requirements set out in the financial provisions of the Withdrawal Agreement. The UK and EU committed to continue working collaboratively on a range of technical issues in recognition of the mutual benefit of smooth implementation of the financial provisions of the Withdrawal Agreement. This initial meeting provided the framework for technical engagement between the parties.

E.43 The first meeting also discussed proposed amendments to several of the operative dates relating to implementation of the financial provisions.[65] These changes were required in the interests of legal certainty and to reflect necessary adjustments as a result of the later date of entry into force of the Withdrawal Agreement than was

65 Article 164(1) empowers the Withdrawal Agreement Joint Committee) to adopt decisions amending that Agreement, provided that such amendments are necessary to correct errors, to address omissions or other deficiencies, or to address situations unforeseen when the Agreement was signed, and provided that such decisions do not amend the essential elements of that Agreement.

foreseen when it was agreed. These proposed changes had the effect of:

- removing redundant references to the year 2019 because the Withdrawal Agreement did not take effect until 2020
- replacing the July reporting dates provided relating to the exit-balances for financial instruments from 2019 to 2020
- altering the payment schedule for return of the UK's share of the paid-in capital of the EIB from the first payment being due on 15 December 2019 to 15 October 2020 (and each year thereafter until 2031)

E.44 Following discussion by the SCFP the Withdrawal Agreement Joint Committee agreed Decision 1/2020 relating to dates given in Articles 135; 137; 143; 144 and 150 of the Agreement. The same Decision also corrected the omission in Article 145 of the Withdrawal Agreement of provisions governing grants under the Research Fund for Coal and Steel that were granted before the end of the transition period to beneficiaries established in the United Kingdom.

E.45 The SCFP also considered the application of Regulation 538/2020 to the UK. This Regulation amended the scope of the MFF so that a special instrument (the Global Margin for Commitments (GMC)) could be used to fund public health emergencies as part of the EU's Covid-19 response. The Withdrawal Agreement guarantees that any amendments made to the Multiannual Financial Framework after withdrawal do not apply to the UK, insofar as they impact upon the UK's financial contributions. This is to protect the UK from any such changes that are made now that we have left. The government continues to hold technical discussions with the European Commission about the amendment to the GMC. The UK recognises and fully respects that the Covid-19 pandemic has required the EU and its member states – and all other countries - to agree emergency economic measures. The UK is supporting the EU's efforts to tackle coronavirus, and will meet its obligations through the financial settlement. However, the government does not intend to go beyond what was agreed in the Withdrawal Agreement, because the UK left the EU before the amendment was adopted.

E.46 A second meeting of the SCFP was held in December 2020. The UK and EU provided updates on the implementation of the reporting obligations underpinning assurance of the financial settlement. The meeting noted positive engagement on the first formal reporting under the Withdrawal Agreement described from paragraph E.34; as well as positive progress towards the March deadline for reporting the 2020 year-end liabilities due under the agreement. The committee also noted that technical discussions of the application of Regulation 538/2020, amending the scope of the GMC, were ongoing; and that the matter had also been discussed in the WAJC. The WAJC is the formal governance mechanism which will be responsible for resolving this issue.

E.47 A third meeting of the SCFP was held in April 2021 to formally note delivery of the second formal reporting package under the Withdrawal Agreement which was provided by the European Commission at the end of March, and the communication on 16 April of the first document specifying the relevant amounts to be paid in 2021 in relation to the settlement of the UK's net liabilities under the Withdrawal Agreement.

E.48 Outside of this formal governance process we have undertaken a wide range of technical engagement on financial reporting with the European Commission's Directorate General for the Budget (DG BUDG) and other officials from the European Commission and its partners. An overview of this engagement is provided in Box E.3.

Box E.3: Technical engagement between the UK and EU

This programme of technical engagement on the financial provisions began in 2020 and is ongoing. During that time we have:

a) held more than 60 meetings with DG BUDG workstream leads, and relevant experts from other parts of the European Commission and its partner institutions, on individual articles in order to agree a shared understanding of implementation requirements

b) discussed and agreed the design of the formal reporting packages provided in July 2020, March 2021 and the invoice sent in April 2021

c) addressed technical queries arising from delivery of these reports

d) held several high-level coordination meetings to ensure that shared objectives and milestones for reporting were met

e) met with representatives of the EIB and its auditors

f) met with the European Court of Auditors (ECA) to discuss the scope and nature of its audit work for the year ended 31 December 2020

E.49 A number of calculation inputs and figures contained within the Withdrawal Agreement are based on estimations or provisional figures, which are subject to adjustment in future years in accordance with the EU's financial regulations or specific provisions within the WA itself. This includes, for example, estimated payments in a given year on RAL commitments and the UK financing share percentage, which will be finalised in February 2022.

E.50 Where this is the case, there will be adjustments in future years once the data becomes definitive. We have agreed with the European Commission a 'true-up' mechanism which allows for adjustments:

- for errors identified by the UK or the European Commission in respect of invoiced amounts
- to correct for adjustments identified during the independent audits of the EU annual accounts and its entrusted entities
- resulting from differences between forecasts and outturn. Formal governance under the WA supports our technical engagement and future corrections in the event of disagreement

Cost of the financial settlement

E.51 Following the publication of the Joint Report from the Negotiators of the European Union and the United Kingdom government in December 2017, the government provided a reasonable central estimate of the size of the financial settlement of €40-45 billion or £35-39 billion based on the exchange rate at the time.

E.52 The financial settlement was originally agreed in December 2017 on the assumption that the UK would leave the EU on 29 March 2019. Due to the extensions to Article 50, the cost of the settlement will be different to the original estimate, as some UK and EU payments that would originally have been paid post-withdrawal were instead paid while the UK remained a Member State. The new estimate is, however, reconcilable with the original estimate when taking these payments into account.

HM Treasury's updated estimate

E.53 In January 2018, the then Chancellor set out a reasonable central estimate for the financial settlement to the Treasury Select Committee. This range valued the settlement at £35-39 billion. Treasury's modelling at the time was consistent with the estimate provided alongside the Joint Report. Since the original estimate, the Treasury has continued to update and improve its modelling, utilising new data and refining assumptions, such as new EU expenditure plans. The key changes since January 2018 are:

- **new budgetary information** – since January 2018 the EU have published three new annual budgets and provided more data on the implementation of expenditure. All information as of 31/3/2021 has been incorporated to provide the latest estimate of the settlement
- **most recent EU published accounts** – the Treasury's most recent estimate incorporates information the EU have provided in their consolidated annual accounts for 2020. These figures inform the 'Assets and Liabilities' component of the financial settlement
- **improved modelling** – The Treasury have been working alongside the Government Actuary Department (GAD) to develop more accurate and sophisticated modelling of certain articles in the Withdrawal Agreement, namely Article 142 (Pensions), and Article 143 and 144 (Financial Instruments)

E.54 The latest estimates are calculated as point estimates. Table E.1 provides a more detailed component breakdown of the Treasury's most recent estimate.

Table E.1: Composition of the financial settlement € billion (£ billion)

Component of the settlement €billion (£billion[1])	Gross payments	Receipts (from EU programmes and assets)	Net	Time period
Budgetary Contributions to end 2020	17.2 (14.7)	-6.0 (-5.4)	11.2 (9.3)	2020
RAL from end 2020	34.0 (29.0)	-10.8 (-9.2)	23.2 (19.8)	2021-26
Assets and Liabilities	9.9 (8.4)	-8.4 (-7.1)	1.5 (1.3)	2020-2065
Total settlement	61.1 (52.1)	-25.2 (-21.7)	35.9 (30.4)	-

1 Based on the spot rate euro/sterling exchange rate on 31st March 2021. The rate was £1 = €1.17.

E.55 Table E.2 provides a breakdown of the main asset and liability items referred to in table E.1. The largest item is the UK's share of the EU's pension liabilities. The European Fund of Strategic Investments and Guarantee Fund for External Action refer to guarantee funds held by the EU in respect of their contingent liabilities for lending undertaken by other parties. As set out in table E.4, the UK also stands behind a share of those contingent liabilities.

Table E.2: Breakdown of assets and liabilities – HMT new point estimate as at 31st March 2021

Component	Asset (€billion)	Liability (€billion)	Net (€billion)	Net (£billion)
European Investment Bank paid in capital	-3.5	-	-3.5	**-3.0**
Financial instruments[1]	-2.1	0.0	-2.1	**-1.8**
Other Assets and Liabilities[2]	-2.8	0.0	-2.7	**-2.3**
Pensions Liability	-	9.8	9.8	**8.5**
Total	-8.4	9.9	1.5	**1.3**

Assets and liabilities shown here are absolute totals and do not reflect repayments.

1 This includes all financial instruments covered by Article 143 and 144 of the Withdrawal Agreement, which includes provisioning funds associated with the European Fund for Strategic Investments and the Guarantee Fund for External Action and EU programme guarantees that have been fully provisioned by the EU Budget (e.g. Innovis).
2 Includes UK share of the 2020 EU budget surplus (Art 136), return of ECB capital (Art 149), financial corrections (Art 140), European Coal and Steel Community in Liquidation (Art 145), EU investment in the European Investment Fund (Art 146).
- In addition to the assets and liabilities mentioned above there a number of contingent liabilities, such as in relation to the EIB and financial instruments covered in Table A.5

*Column totals do not equal the sum of individual items due to rounding and spending not attributable to any heading.

HM Treasury's new point estimate in relation to the original range of the settlement

E.56 The new estimate is presented in Table E.3 to enable comparison with the original reasonable central range. Net contributions during the Article 50 extension are separately identified to support comparison on a like-for-like basis. The new point estimate of £30.4 billion in Table E.1, adjusted for

Article 50 extension, falls within the range of the original reasonable central estimate.

Table E.3: Comparison of original range to new HM Treasury point estimate

Component of the settlement (billion)	Original Range	Treasury point estimate (31st March 2021)
Net Budgetary Contributions to end 2020	€17-18	€19.0
Of which: Contributions over Article 50 Extension	-	€7.8[1]
Contributions over Transition Period	-	€11.2
RAL (net) from end 2020	€21-23	€22.3
Assets and Liabilities	€2-4	€2.4
Original Settlement Range	€40-45	€43.8
	£35-39	£37.3[2]

1 Estimated contributions and receipts, sent and received by the UK over the Article 50 Extension, April 2019 - January 2020 (£6.9 billion). Subtracting £6.9 billion in net payments from the £37.3 billion point estimate at 31 March 2020 gives the £30.4 billion net cost of the financial settlement set out in table E.1.

2 Original range is based on spot rate euro/sterling exchange rate at the time of the Joint Report in December 2017, £1=€1.13. The Treasury sterling point estimate at 31st March 2020 is based on the spot rate euro/sterling exchange rate on 31st March 2021, £1 = €1.17.

E.57 As set out from paragraph E.21 the UK made its first scheduled payment under the Withdrawal Agreement at the end of June 2021. Further equal payments will be made at the end of each subsequent month of the invoice period and will continue to reduce the estimate of the UK's outstanding net liability provided in the statement. The Treasury is required to recognise a provision in its annual accounts for 2020-21 representing its liability for these amounts. However, because the reporting date for the statement is 31 March 2021 these payments are not reflected in Tables E.1 to E.3 and will be reported in detail from next year.

Treatment of the financial settlement in government accounts

E.58 The UK's contributions to the EU Budget in 2020, up until February 2020 were accounted for in the Consolidated Fund accounts, as was the case when the UK was a member state. Payments to the EU after 31st March 2021 will be accounted for in HM Treasury's Accounts.[66] These include our obligation to outstanding commitments and liabilities, as well as accounting for the return of the UK share of EU assets.

E.59 Payments of receipts from the EU to UK entities are treated in national and government accounts in different ways, depending on whether a government body administers those receipts. Receipts that are administered by a government body are classified as public sector receipts in public expenditure statistics and are typically reported in the administering department's accounts. Although they are classified as 'public sector' receipts, they

66 With the exception of new payments of UK liabilities related to Traditional Own Resources related to the period up to the end of 2020, in accordance with s.20 of the European Union Withdrawal Agreement Act 2020.

are in fact typically destined for the private sector (such as CAP, paid by managing authorities to the private sector). The remaining receipts received by the UK are paid directly from the EU to private sector beneficiaries and these funds do not flow through the public finances.UK central government accounts are prepared in accordance with the HM Treasury Financial Reporting Manual (FReM) and the Government Resources and Accounts Act 2000. The accounting policies contained in the FReM apply International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector context.

E.60 HM Treasury Accounts for 2020-21are due to be published mid July 2021. The Treasury will be required to recognise a provision in its annual accounts for 2020-21 representing its liability for the amounts it will need to pay to the EU after 31 March 2021. This will include, for example, the UK's share of the EU's outstanding commitments at the end of 2020 (the so-called RAL). This will not reflect the complete financial settlement and will therefore not present the 'cost' of the financial settlement, for the reasons discussed below. HM Treasury accounts will also disclose other contingent items relating to EU financial obligations covered by the Withdrawal Agreement.

E.61 The return of the UK's paid in capital in the European Investment Bank appear in the HMT

Annual Resource Accounts. In addition, the contingent liability the UK maintains under the Withdrawal Agreement will be included in HM Treasury accounts in respect of any potential call after 31st March 2021 as any such call after this point would have to be funded from HM Treasury's Supply Estimates.

E.62 HMT and other departmental resource accounts are consolidated into the Whole of Government Accounts (WGA). The UK's contributions to the EU budget are recognised in the WGA as a grant expense as the amount payable to the EU after the UK's rebate has been applied. EU grants and subsidies paid by the UK government to third-party recipients are also recognised as a grant expense, but the EU reimburses the UK for this expenditure.

E.63 The receivable in respect of the UK's former shareholding in the European Investment Bank is recognised as a financial asset and remote contingent liabilities relating to the UK's membership are also disclosed in WGA. However, UK customs duties remitted to the EU (called Traditional Own Resources) are excluded from WGA because under the accounting standards the UK government is judged to be acting as the agent of the EU in collecting these revenues.

E.64 Accordingly, this annex provides a more complete view of the financial settlement, including both remittances to the EU and receipts which would not otherwise appear in government accounts.

Contingent liabilities

E.65 The table below sets out EU related contingent liabilities disclosed as remote contingent liabilities in the Consolidated Fund Accounts. Under the terms of the Withdrawal Agreement, the UK will maintain these contingent liabilities to the EU. Contingent liabilities refer to the present value of a payment obligation with uncertain value or likelihood of crystallising; or possible obligations based on uncertain future events. The EU guarantees financial operations that its 'Implementing Partners', predominantly the EIB and EIF, invest in. This creates a potential commitment to reimburse any future losses on the financial operations that the implementing partners incur. The UK under articles 143 and 150 remains liable for its share of the losses on financial operations approved before 31 January 2020.

E.66 For the financial operations covered under Article 143, a proportion of the contingent liability is provisioned from the EU Budget under budgetary guarantees that the UK contributed to whilst part of the EU. For any losses greater than the amount in budgetary guarantees, the UK would have an obligation to reimburse the EU. In the case that the budgetary guarantees are sufficient to reimburse the losses on the financial operations, any amounts not used will be returned to the UK creating a net financial benefit to the UK.

E.67 Similarly, under Article 150, the UK remains liable for the financial operations approved by the EIB before the withdrawal date. The UK has paid in capital in the EIB that is being returned to the UK on a yearly basis. The contingent liability is in the form of the callable capital subscription to the EIB. The EU may call upon this if there are losses on financial operations greater than the paid in capital.

Table E.4: EU related contingent liabilities from the Consolidated Fund Accounts 2019-2020

(£million)	At 31 March 2020	At 31 March 2019
EIB: Callable capital subscription	31,645	30,643
European Financial Stabilization Mechanism	6,593	6,268
Balance of Payments Facility	241	411
Third countries	2,103	2,099
European Fund for Strategic Investments	1,439	875
Other (macro-financial assistance, EIB lending, Euratom)	181	210
Total Loans Guaranteed by the EU Budget	10,557	9,863

Source: Consolidated Fund Account 2019-20

E.68 Further details on these remote contingent liabilities are set out in the Consolidated Fund Accounts 2019-20. HM Treasury Accounts 2020-2021will also provide information on contingent liabilities related to the financial settlement.

OBR forecast

E.69 Since March 2018, the OBR have produced an estimate of the size of the financial settlement at each Spring Statement/Autumn Budget. This estimate is reported in their Economic and Fiscal Outlook (EFO), which is laid before Parliament. The most recent estimate was published in the March 2021 EFO and stood at £34.1billion.[67]

E.70 There are some important differences between the OBR forecast and the Treasury's estimate.

- **modelling and data sources:** Unlike the OBR's estimate, the Treasury's revised estimate uses a combination of public and non-public sources. Non-public data sources can provide more granular and up to date data. For example, using EU monthly Budget implementation data provided to the UK and member states enables more granular bottom-up modelling of the RAL

- **exchange rate:** The OBR uses a forward-looking exchange rate forecast, while the government

67 Office for Budget Responsibility, Economic and fiscal outlook, March 2021, CP387 https://obr.uk/efo/economic-and-fiscal-outlook-march-2021/

does not have a target for the Sterling exchange rate and does not generally comment on currency movements. The new estimate uses the spot rate at the end of the 2020/21financial year to align with the rate used in HMT departmental Resource Accounts. The exchange rate at the end of each financial year will be used in future editions of this publication, now that we have left the EU

- **pensions liability:** The OBR does not discount any aspect of the financial settlement. The OBR forecast future public expenditure flows from the financial settlement as they would in their fiscal forecast. In contrast, and in line with the 2017 reasonable central estimate, the Treasury's estimate continues to use a discounted valuation of the UK's EU pensions liability. The effect of discounting this liability is significant because the future cash flows are spread over many decades into the future. The Withdrawal Agreement provides the option for the UK to settle pension obligations early (if the UK so choses), based upon a discounted amount. This distinction in methodology is the largest source of difference between the two estimates

Table E.5: Comparison between Treasury estimate and the OBR forecast

	(£billion)
OBR estimate (2021 Spring Budget)	34.1
Exchange rate differences	-0.9
Discounting for Pensions Liability	-3.0
Modelling and data source differences	0.3
HM Treasury estimate (31st March 2021)*	30.4

*Column totals do not equal the sum of individual items due to rounding.

Factors affecting the size of the settlement

E.71 In conducting sensitivity analysis on the financial settlement, the Treasury has considered the key individual variables within the settlement and the impact that a change in individual variables would have on the overall settlement value.

E.72 The final value of the settlement, by its nature, cannot be known definitively at present, since the settlement requires the UK and EU to pay only those amounts that fall due, rather than on the basis of a forecast. However, not accounting for the reductions arising from the extension to the Article 50 period as described above, the Treasury considers it unlikely that the final value, which will not be known for some years, will fall outside the original estimated range.

E.73 The following are the main factors that could affect the value of the settlement. In future reports, if the Treasury considers the actual settlement is likely to fall outside the original estimated range, it will set this out with an explanation of the factors that could lead to this.

Limits on EU expenditure and revenue

E.74 The ceilings of the Multiannual Financial Framework set the limits for how much the EU was able to commit over 2014-20, and therefore ultimately spend.

E.75 The settlement freezes the ceilings of the Multiannual Financial Framework (MFF) 2014-20 for the UK, so that any changes agreed by Member States after the UK's withdrawal will not impact on the UK. This protects the UK not only during the Transition period, but for the lifetime of the settlement. The UK obligations to the EU's outstanding commitments at end-2020 cannot be larger than the limits agreed by the UK while it was a Member State.

E.76 The terms of the calculation of the UK's contribution, as set out in the Own Resources Decision, is also frozen post-withdrawal. This protects the UK from changes to rules for calculating revenue (including the UK's rebate) after withdrawal impacting on the UK's financial contributions.

E.77 The EU proposed a range of budgetary responses to respond to the pressures of COVID-19, which increased in-year commitment appropriations for the EU annual budget 2020. However, in several areas the EU has confirmed that the UK, because of the protections secured in the WA, has no liability for additional contributions because they arise in respect of increases to the MFF ceilings that were agreed while the UK was a Member State. The UK is not liable for:

- Support to mitigate Unemployment Risks in an Emergency (SURE), which does not apply to the UK. The UK will neither receive financing from this programme, nor will it accrue any new contingent liabilities as a result of this programme.[68]
- The wider €540bn Recovery Fund support package announced by the Eurogroup on 9 April 2020.[69]
- Proposals to borrow a further €750bn on the capital markets between 2021-24, subsequently announced at the end of May 2020, which will be funded through the next MFF (2021-27) and which are consequently outside of the scope of the financial

68 https://data.consilium.europa.eu/doc/document/ST-7161-2020-INIT/en/pdf

69 https://www.consilium.europa.eu/en/press/press-releases/2020/04/09/report-on-the-comprehensive-economic-policy-response-to-the-covid-19-pandemic/

settlement. These proposals are known as the 'NextGenerationEU' stimulus package.[70]

Decommitments

E.78 A key principle of the financial settlement is that the UK will only pay towards EU obligations that actually materialise. Both Treasury and OBR forecasts of the settlement therefore include an estimate of the EU spending that will be decommitted (planned, but ultimately never spent).

E.79 The effect of a 1% absolute change in decommitments on the HM Treasury net estimate is estimated to be £208 million.

UK receipts

E.80 Under the financial settlement, the UK will continue to benefit from the implementation of the budget as if it had remained a Member State over the entirety of the current multiannual financial framework (subject to the protections described at paragraph E.45 and E.76) This means that, subject to the normal audit and accountability requirements, all EU spending that was committed to the UK before the end of 2020 will be paid, even if those payments are due to be made in future years.

E.81 The forecast for UK receipts under the Financial Settlement is set out in Table E.1. This forecast

70 https://ec.europa.eu/info/strategy/recovery-plan-europe_en

assumes the UK's share of receipts from each heading was the same percentage as that of previous years of this MFF.

E.82 Around three quarters of UK receipts are fixed automatically each year, through EU regulations or operational programmes. While subject to audit and potential correction, these amounts are generally less sensitive to year-by-year variation.

E.83 The remaining quarter of receipts are received through competitive grant programmes such as Horizon 2020, and by nature vary from year-to-year. Grants are assessed by neutral experts on the merits of the bid, and this remains the case for the UK under the terms of the Withdrawal Agreement.

E.84 The effect of 1% change in the non-allocated receipts forecast on the HM Treasury net estimate is estimated to be £31 million.

Financing Share

E.85 The UK's financing share of the EU budget is calculated annually and determines the amount of UK contributions to the EU Budget (taking into account the rebate) relative to all Member State contributions to the EU Budget. A definition of financing share is provided in the Glossary at A.6

E.86 Under the terms of the Withdrawal Agreement, the UK's financing share in 2020 was determined broadly as if the UK had remained a Member State. Beyond 2020, the UK's financing share will be equal to the ratio of UK own resources transferred to the EU over 2014-20 to total own resources transferred over 2014-20, taking into account the revenue adjustment exercises in 2021 and 2022. The UK's provisional financing share based on this methodology, but subject to adjustment in 2022, is 12.36%.

E.87 Since nearly all the UK's own resources contribution to the EU between 2014 and 2019 has already been determined, there is unlikely to be any significant change to our current estimate of the overall 2014-20 financing share.

E.88 The effect of a 1% change[71] in the UK's financing share, which is applied to all post-Transition Period obligations, on the HM Treasury estimate is £382 million.

Exchange rates

E.89 Under the terms of the financial settlement, the UK continued to make its budget contribution in 2020 in sterling, but began settling its post-2020 obligations in euro. As a result, any movements in the euro-sterling exchange rate may affect the value of the settlement:

71 This is equivalent to an increase in absolute terms of over 0.1% in terms of the UK's share of post Transition obligations.

- over 2020, changes in the value of sterling affected the UK's financing share, as the UK's share of euro-denominated VAT and GNI bases will change. The sterling value of UK payments and receipts will also change
- after 2020, changes in the value of sterling will still affect UK payments and receipts, but will no longer affect the UK's financing share, which is based on the average over 2014-20

E.90 The government does not have a target for the sterling exchange rate and does not generally comment on currency movements. In managing exchange rate risk with respect to public spending it applies the principles of Managing Public Money.

E.91 The effect of a 1% change in the sterling/euro exchange rate on the HM Treasury net estimate is estimated to be £203 million.

Balance sheet items

E.92 The main EU liability included in the financial settlement is in relation to EU pensions and other employment related benefits accrued by the end of 2020. These are predominantly unfunded defined benefit schemes where the final amounts paid to beneficiaries are affected by a number of factors, including the final salaries of the employees, their years of service and the length of time they live in retirement. The amount the UK pays will be affected by these factors. However, because the UK is only required to pay these amounts as they fall due many of the uncertainties in estimating pension liabilities (like the choice of discount rate used to convert the future flows into a lump sum amount) will not affect what the UK pays, unless the UK chooses to settle the obligation early, as provided for in the Withdrawal Agreement.

E.93 The UK will continue to stand behind contingent liabilities arising from EU financial operations approved before withdrawal. Several of these instruments have associated guarantee funds. These funds are held on the EU's balance sheet. The extent of returns to the UK from these funds will depend on the financial performance of the funds and the underlying investments that are covered by the guarantees.[72]

E.94 The effect of 0.1% decrease in the discount rate applied to the UK share of EU pensions increases the estimate of the financial settlement by £70 million.

72 HMT uses a model to produce a base-case assessment of cashflow in respect of financial instruments. Certain assumptions can, if required, be updated to produce cashflow on a stressed basis, including changes to credit ratings, recovery rates and returns on assets/funds.

Domestic replacements for EU spending

E.95 As receipts from the EU diminish, there will also be a direct cost to the public finances from any new domestic spending to replace financial support (to the public and private sectors) currently provided by receipts from the EU budget, or for the administration of services and functions currently provided by the EU.

E.96 Prior to the 2020 Comprehensive Spending Review, the government had already made commitments to replace certain EU-funded programmes, for example guaranteeing the existing annual budget for farmers in each year of this Parliament, and announcing that funding would be allocated to a UK-wide Shared Prosperity Fund to tackle deprivation and support local economic recovery by driving economic growth.

E.97 At the CSR 2020, the government provided funding for both association costs and domestic replacement programmes in 2021/22. Settlements for future years will be determined at the next Spending Review.

Off-budget funds outside the financial settlement

E.98 There are a number of areas where funds, mechanisms and organisations have been established outside the EU Treaties through separate international agreements but are managed by EU institutions or are in close alignment with EU policies. The Withdrawal Agreement makes provision for these to ensure there is certainty on how they will be treated. These mainly relate to international development funding, where UK contributions are treated as Official Development Assistance (ODA) and count towards the UK's ODA spending target. They are set out in the Department for International Development's (DFID, merged with the FCO in September 2020 as the new FCDO – Foreign Commonwealth and Development Office) DEL spending estimate and accounts.[73]

E.99 The government considers payments and receipts in relation to these to be outside the financial

73 Under the Withdrawal Agreement, the UK will honour its commitment to the current and previous European Development Funds. The EDF derives from the European Union's Cotonou Partnership Agreement. The eleventh and latest EDF covers the commitment period from 1 January 2014 to 31 December 2020, though payments relating to these commitments will continue to flow after 2020. It provides support to 79 African, Caribbean and Pacific (ACP) countries and Overseas Countries and Territories (OCTs) to eradicate poverty, support sustainable development and integrate ACP countries into the world economy. UK Overseas Territories will benefit from the current and previous EDFs until their closure. Each year, the European Commission is legally obliged to provide statements of forecasted commitments, payments and the annual amount of the calls for contributions to be made in that year and the following two budget years to both the EDF and its ACP Investment Facility, managed by the EIB. The Commission also provides forecasts for a further two years, which are non-binding estimations.

settlement. Nevertheless, the government is committed to pay its share of the to the European Development Fund (EDF) and bilateral contributions to the Facility for Refugees in Turkey or EU Trust Funds as part of the Withdrawal Agreement.

Table E.6: Outstanding off-budget development contributions, as at 31 March 2021

Outstanding off-budget contributions (as at 31 March 2021)	(€ millions)	(£ millions)[4]
European Development Fund[1]	2,268	1,932
Facility for Refugees in Turkey[2]	75	64

1 HM Treasury calculations using EDF internal agreements and EU Commission annual communications forecasting commitments, payments and contributions from Member States.

2 Combined total of the UK's outstanding contribution to the first tranche of the Facility (which is sourced from DFID's Development Tracker: https://devtracker.dfid.gov.uk/projects/GB-GOV-1-300287/documents) and the UK's share of the second tranche, based on internal DFID/EU Commission figures.

3 EU Commission website on EU Emergency Trust Fund for Africa: https://ec.europa.eu/trustfundforafrica/content/trust-fund-financials_en

4 Based on the spot rate euro/sterling exchange rate on 31st March 2021, £1 = €1.17.

European Development Fund

E.100 The most recent statements from the European Commission details contributions in 2020 from Member States and forecasts of commitments, payments and contributions from Member States for 2021 and 2022; and non-binding forecast for the years 2023-2024. The forecast UK contributions are summarised in Table E.7. Although the European Commission has not yet produced contribution forecasts for years after

2023, the government expects EDF contributions to continue to c. 2027 as projects the UK is committed to are implemented and finalised.

E.101 The EIB African, Caribbean and Pacific (ACP) Investment Facility (IF) managed by the EIB focusses predominantly on private sector development in ACP countries (and a limited number of EU Overseas Territories) and is funded by EU Member States through the EDF. A total of €3.7 billion[74] of EDF contributions has been committed to a revolving fund in the IF, which invests in assets (e.g. loans, equity) that generate reflows to the facility for reinvestment on a self-sustaining basis. The Withdrawal Agreement confirms that the UK's share of the facility will be returned to the UK as the investments mature, unless agreed otherwise. As at end-2020, the UK had contributed €396 million[75] (£337 million) to the facility through our share of the EDF. At the end of 2020, the UK's share is estimated to be around €502 million[76] (£428 million), less any loss.

E.102 Under the terms of the Withdrawal Agreement, the UK will also remain liable in respect of its guarantee to EIB own resources lending to ACP

74 https://www.eib.org/en/projects/regions/acp/applying-for-loan/investment-facility/index.htm ; https://www.eca.europa.eu/Lists/ECADocuments/SR15_14/SR_INVESTMENTS_EN.pdf

75 Based on internal communication from EIB ACP IF Secretariat communications to shareholders.

76 This figure is based on the UK's share of total Investment Facility for the 9th, 10th and 11th EDF's, as detailed in their respective Internal Agreements.

countries and the OCTs, as laid out in the EDF financing protocols under the Cotonou Agreement. Any calls on this guarantee would need to be met collectively by the UK and other EDF contributors in proportion to their respective shares in the agreements. Subsequently, the UK will be entitled to any share of amounts recovered in the event of a guarantee pay-out. As at 31 December 2020, the UK's total contingent liability on EIB loans under these guarantees was €224 million[77] over a period up to and including 2050, but this may increase further as more EIB loans are signed under the agreements. Under the terms of the Withdrawal Agreement, the UK will honour its contingent liabilities under this guarantee in full, which includes loans approved up to the end of 2020.

Table E.7: UK contributions and forecast contributions to EDF, as at 31 March 2020

Year	(€ millions)	(£ millions)
2021	587	500
2022	411	350
2023	308	262
2024	250	213

Source: European Commission Communication October 2020.
Based on the spot rate euro/sterling exchange rate on 31st March 2021, £1 = €1.17.

77 EIB-Member State - Guarantee Agreements (Cotonou I II III) - UK – 2020 2nd half year report.

EU Trust Funds and the Facility for Refugees in Turkey

E.103 The UK will also honour commitments it made to the Facility for Refugees in Turkey and the EU Trust Funds. As with EDF, these contributions count as ODA, with bilateral contributions currently paid using powers provided in the International Development Act 2002.

Non-developmental outstanding off-budget contributions

E.104 The Withdrawal Agreement also set out the United Kingdom's obligations to the financing of the European Defence Agency (EDA), the European Union Institute for Security Studies (EUISS), and the European Union Satellite Centre (EUSC), as well as to the common costs of Common Security and Defence Policy operations, until 31st December 2020.[78]

E.105 In total the UKs outstanding off-budget contributions for the above agencies and CSDP common costs came to €21.13 million in 2020. As with development contributions, the government considers payments and receipts in relation to these to be outside the financial settlement. It did not meet the cost of contributions

78 Article 156 WA

through authority granted by the EU Withdrawal Agreement Act 2020.

E.106 The Withdrawal Agreement also sets out the United Kingdom obligations to funding the pension liabilities for the personnel of the EDA, the EUISS, and the EUSC as well as the liabilities arising from the liquidation of the Western European Union (WEU), to the extent they were provisioned on 31 December 2020. The total invoiced UK liability was €55.92 million (£47.64 million) which was settled by the end of June 2021.[79]

Future reporting on the financial settlement

E.107 During the UK's membership of the EU, the government laid before Parliament this annual statement on European Union Finances that presented information on our contributions and receipts. The government has committed to report regularly on the financial settlement and intends to continue reporting on outstanding net liabilities under the Withdrawal Agreement. Nevertheless, the format and scope of the statement is likely to change significantly from next year as the importance of receipts in respect of the UK's period of EU membership reduces.

79 Article 157 WA

Short-term public expenditure costs of EU exit

E.108 HM Treasury has provided additional funding to departments and the devolved administrations to prepare for and then deliver the UK's departure from the EU, the following transition period and subsequently the costs of the post-transition period. In total over £12 billion of additional funding has been made available by the government for this purpose since 2016.

E.109 The additional funding made available to department includes:

- Autumn Budget 2016 confirmed initial allocations of over £400 million funding across 16-17 to 19-20
- Autumn Budget 2017 committed an additional £3 billion to departments split evenly between 2018-19 and 2019-20. Funding allocations for 2018-19 were confirmed in the Chief Secretary to the Treasury's Written Ministerial Statement of 13 March 2018
- Autumn Budget 2018 increased the funding available in 2019-20 by a further £500 million (taking the total available in that year to £2bn). Allocations of this were confirmed in the Chief Secretary to the Treasury's Written Ministerial Statement of 18 December 2018

- in August 2019, £2.1bn was made available for “no deal” preparations in 2019-20. Before this allocation some departments also made direct claims on the Reserve to support “no-deal” preparation in 2019-20
- the Spending Round 2019 committed £2 billion of core funding to departments for post-Brexit delivery in 2020-21
- Supplementary Estimates 2020-21 confirmed reserve claims for delivery of the UK’s departure from the EU totalled £1.7bn in 2020-21. This included the funding awarded as part of the 2020 Borders Process, which was announced on 12 July 2020 to provide funding for border infrastructure, jobs and technology to ensure border systems were fully operational after the end of the transition period
- the Spending Round 2020 committed £2.4bn of core funding to departments for post-EU Exit delivery in 2021-22

E.110 Table E:8 below sets out funding provided to prepare for and then deliver the UK’s departure from the EU in financial years 2016-17 to 2021-22. Figures are shown in £m

Table E.8: Departmental allocations: EU Exit funding allocations 2016-17 to 2021-22

Department	16/17	17/18	18/19	19/20	20/21	21/22	Total
Cabinet Office	0	6.6	49.4	187.9	195.6	43	**482.5**
Competition and Markets Authority	0	1	23.6	20	21.5	16.8	**82.9**
Department for Business, Energy and Industrial Strategy	0	35.1	324.6	216.9	194.7	35.5	**806.8**
Department for Culture, Media and Sport	0	3	26.2	31.9	30.6	28.1	**119.8**
Department for Education	0	0	0	8.4	0	0	**8.4**
Department for Environment, Food and Rural Affairs	0	67.5	310	567.8	557.1	571.7	**2074.1**
Department for Exiting the European Union**	50.9	93.6	93.5	89.1	0	0	**327.1**
Department for International Trade**	8.7	53.6	97.3	162.8	0	0	**322.4**
Department for Transport	0	19.6	75.8	305.4	266.6	63	**730.4**
Department of Health and Social Care	0	0	21.1	381.5	116	95	**613.6**
Department for Work and Pensions	0	0	0	116.7	15.3	16	**148**
Food Standards Agency	0	0.9	14	19	14.6	3	**51.5**
Foreign and Commonwealth Office**	0.1	8.3	36.9	53.6	45.8	60	**204.7**
HM Revenue & Customs	0	46.9	259	555	999.1	1,033.8	**2893.8**
HM Treasury	0	14.1	24.8	51.1	38.7	31	**159.7**
Home Office	0	60	400.5	605	792.8	427	**2285.3**
Law Officers' Departments	0	0	0	2.7	2.7	3.6	**9**
Ministry of Defence	0	0	12.7	17.9	0	0	**30.6**
Ministry of Housing, Communities and Local Government	0	0	0	74.9	15	0	**89.9**
Ministry of Justice	0	0	17.3	34.7	42.8	30.7	**125.5**
Northern Ireland Office	0	0.3	0.4	3.8	1.1	0	**5.6**
Office for National Statistics	0	0	2	2.4	2.4	0	**6.8**

*

Department	16/17	17/18	18/19	19/20	20/21	21/22	Total
NIE inch PSNI (direct non-Barnett)	0	0	0	37.6	30.3	0.8	68.7
Scotland Office	0	0.3	0.3	0.3	0.3	0	1.2
Single Intelligence Account	0	0	0	12.8	0	0	12.8
The National Archives	0	0	1.2	2.1	2.1	0	5.4
The Supreme Court	0	0	0	0.5	0.4	0	0.9
Wales Office	0	0.1	0.3	0.3	0.3	0	1
Scottish Government (direct non-Barnett)	0	0	0	20.2	N/A	0	20.2
Wales Government (direct non-Barnett)	0	0	0	13.3	N/A	0	13.3
Total	59.7	410.9	1790.0	3595.6	3,385.8	2,459	11,701.9
Barnett consequentials* **	**16/17**	**17/18**	**18/19**	**19/20**	**20/21**	**21/22**	**Total**
Northern Ireland Executive	-	2.3	15.2	39.2	31.2	28	115.9
Scottish Government	-	6.6	37.3	102	81.7	48.8	276.4
Welsh Government	-	3.7	21.4	59.5	46.1	27.5	158.2
Total	-	12.6	73.9	200.7	159	104.3	550.5
Office for National Statistics	0	0	2	2.4	2.4	0	6.8

*This table excludes relevant expenditure funded by departmental reprioritisation of existing resources. Final budgets are confirmed in the relevant Main or Supplementary Estimate. Expenditure from within those budgets is confirmed in departmental Annual Reports and Accounts

**This table does not include any additional Reserve claims for 2021-22, which will be confirmed at Supplementary Estimates 2021-22.

***Foreign, Commonwealth and Development Office (FDCO) figures from before 2020-21 refer to Foreign and Commonwealth Office (FCO) funding. In 20/21, the FCO merged with the Department for International Development to form the FDCO.

****This table shows Barnett funding applied on a policy basis of EU Exit funding for UK government departments 2017-18, 2018-19 and 2019-20. At the 2019 and 2020 Spending Reviews, Barnett was applied in the usual way to departmental settlements for 2020-21 and 2021-22.

F. Annex F

The Trade and Cooperation Agreement

Future relationship with the EU

F.1 Part 5 of the TCA sets out the cross-cutting terms and conditions for the UK's participation in EU programmes and access to EU programme services. These provide for a fair and appropriate financial contribution towards the programmes, fair treatment of UK participants, balanced provisions to ensure the sound financial management of programme funds, and appropriate governance arrangements.

F.2 Part 5 of the TCA is complemented by a financial annex specifying the implementation of the financial conditions and the Joint Declaration on Participation in Union Programmes[80], which includes draft protocols establishing an association of the United Kingdom for participation in Horizon Europe, Euratom Research and Training (R&T), Fusion for Energy, and Copernicus, as well as access to services from the EU Space Surveillance and Tracking programme for the duration of the 2021-27 MFF funded programmes. These were agreed

80 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/948105/EU-UK_Declarations_24.12.2020.pdf

in principle and will be adopted by the Specialised Committee on Participation in Union Programmes at the earliest possible opportunity.

F.3 The UK will make a proportionate contribution based on the Horizon Europe, Copernicus, Euratom R&T, and Fusion for Energy programme budgets and an administrative contribution for the cost of running these programmes. These costs must be within overall ceilings set up by the EU's 2021-27 MFF and the UK has protections in place, including against large increases to the programme budgets. The UK is not required to make a financial contribution to access services from the EU Space Surveillance and Tracking programme.

F.4 The exact cost of participation to Horizon Europe, Copernicus, Euratom R&T and Fusion for Energy will be determined annually in line with the terms set out in the agreement and reported by government in departmental accounts The UK will also be a beneficiary from these programmes as participants will receive receipts, which represent a financial benefit to the UK but are not recorded in the government accounts.

F.5 In the *Joint Declaration on Participation in Union Programmes and Access to Programme Services*, the UK and the EU recalled their commitments to the Peace Plus programme which will be the subject of a separate financing agreement. The government will deliver the Peace Plus programme for the 2021-27 MFF as part of the UK's unwavering commitment to uphold the hard-won peace in Northern Ireland. The government is working with the European Commission and the Irish Government to shape the programme. The Peace Plus Financing Agreement will set out the UK's total and annual financial contributions to the programme, balanced provisions to ensure the sound financial management of programme funds and appropriate governance arrangements.

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This document can be downloaded from www.gov.uk

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