

Balance of competence review: EU Budget

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Role of institutions and budget system

1 What do you see as the rationale for having an EU budget?

There are several dimensions to a rationale for an EU budget, though ultimately the issue is a political one, rather than a purely rational one. It is also important to stress that the rationale for an EU budget cannot be perceived in comparable terms to that for national budgets in terms of purpose, structure or size.

At a fairly prosaic level, there is a rationale for a budget to support the implementation of common policies and tasks decided by the Union and contained in the Treaties – notably Cohesion policy and the CAP (what the scope and nature of these policies should be is an underlying question). There are also arguments that some spending is necessary to accompany legislative measures flowing from the Treaties. It might have been thought that the role of the budget would grow as the tasks assigned to the Union have grown, but the extent to which this has happened is rather limited and it could be said that the role of the budget in promoting integration has lessened rather than grown through time.

Partly flowing from the Treaty, but also for other reasons (equity, 'solidarity', pragmatism), there are arguments in favour of spending on Cohesion policy aimed at reducing economic disparities and facilitating the participation of all Member States in an integrated market. Under the major 1980s reform, Cohesion policy was implicitly linked to the completion of the internal market and targeted at disadvantaged countries and regions; this has also brought indirect benefits to the more prosperous Member States through increased business opportunities (though Cohesion policy now applies in all regions, albeit at different levels of intensity).

At a more theoretical level, the basis for an EU budget has been the subject of much discussion in the academic literature, drawing, among other things, on aspects of public economics and fiscal federalism.¹ This points towards a justification for EU level spending to address common challenges where either countries acting alone lack the critical mass to do so or where there is a genuine cross-border dimension – examples could include energy security, environmental issues, climate change, migration; Cohesion policy expenditure in the most disadvantaged countries is also often cited in this context.² In practice, with the notable exception of Cohesion policy, these are not significant elements of expenditure in the current EU budget, so there is a disconnect between what theory suggests might be rational and the structure of the budget in practice.

This disconnect is rooted in history and politics and has arguably been calcified by the net balance considerations that dominate the negotiation of the MFF. The CAP finds its origins in post-war food shortages but also in political compromises that enabled German access to French markets and support for the French agricultural sector.³ Cohesion policy essentially developed from the

¹ See, for example, Figueira, F. (2009) How to Reform the EU Budget? A Methodological Toolkit, Swedish Institute for European Policy Studies, report no. 5.

² However there are mixed views on the targeting of policy, notably its availability in all regions, irrespective of prosperity.

³ See eg Swann, D. (multiple editions) The Economics of the Common Market.

establishment of the ERDF in 1975 in response to UK concerns that it would not benefit significantly from the CAP;⁴ Cohesion policy has grown significantly since its inception, partly fuelled by successive enlargements, though its initial focus on disadvantaged regions has been supplanted in favour of an all-region economic development policy. These two spending areas (CAP and Cohesion) account for the bulk of the EU budget and, together with so-called own resources (and associated 'corrections'), are at the nub of the lengthy debates on the MFF. Moreover, the structure of the budget and the defence of national interests in a context where the MFF is agreed by unanimity contribute to a situation where the *status quo* dominates and changes are at the margins. As such, the ultimate shape of the budget is driven by a 'bottom line' in terms of national net contributions/receipts rather than policy-driven considerations of what budget is needed and to what end. This is reflected, for example, in the fact that Cohesion policy *allocations* are negotiated quite separately from the *substance* of policy, the former being a key (predictable) element in determining net balance positions and subject to considerable fine tuning to deliver on deliver target levels of contributions or receipts.

2 What are your views on the appropriate roles of national and European institutions, particularly the voting rules and relationship between the domestic and European Parliaments, the Council and the Commission, in agreeing the EU budget?

In a situation where EU resources are in the main derived directly from national budgets it is difficult to envisage a situation where the MFF could be decided other than by unanimity in Council. The role of the President (van Rompuy) in the latest negotiations was interesting, may help prevent some of the discontinuity between (national) Presidencies and may also affect the role of the Commission, though it remains to be seen whether some of the larger Member States would allow the President to play such a role under their presidencies. There are, however, no signs that the role of the President has the capacity to alter the essentially path dependent nature of the budget structure.

The input of the European Parliament added several months to the process of agreeing the MFF. While some aspects of the agreement were important (in relation to the annual budget, for example), it contributed to the overall atmosphere of brinkmanship, which was arguably counterproductive. The role of national parliaments is a matter for Member States.

3 What are the advantages and disadvantages of having unanimously-agreed long-term budget periods? How long should they be?

The advantages are arguably two-fold: (i) predictability for strategic planning purposes – an important criticism of the pre-1988 period was the extent of ad hoc decisions and the inability to make long-term plans owing to absence of long-term budgeting. (ii) The gruelling negotiation involved in the MFF could not be undertaken (much) more frequently. The key disadvantages are the lack of flexibility to respond to changing circumstances.

It is questionable whether anyone has the appetite for (much) shorter budget periods, though there is a case for aligning these with the Commission and EP mandates. A key difficulty is that debates on the MFF scarcely cease mid-term – debates on the 2014-20 MFF arguably started with the 2008/9 budget review.

⁴ Wallace, H (1977) The Establishment of the European Regional Development Fund: Common Policy or Pork Barrel? In Wallace, H and Wallace, W (eds) Policymaking in the European Community.

4 What are the advantages and disadvantages of the existing system of commitments and payments? Can you think of ways to improve that system?

There is merit in the system of commitments and payments with the former essentially decided as part of the MFF negotiations, but not in having both multiannual and annual budgeting as a major source of controversy. In one sense the 'real' budget is the annual one insofar as it determines the cash available; however, the current structure lacks coherence when spending has already been endorsed in principle through the MFF process and risks marking a return to the levels of uncertainty that underpinned the introduction of multiannual budgeting in the first place. One of several major presentational issues with the EU budget system is the confusion between the annual and multiannual processes in the public imagination; the scale of spending and the UK contribution also tend to be massively overestimated. There seems to be little political or media appetite for improving the quality of information or debates on this and dispelling some of the myths surrounding the scale of EU expenditures.

5 What are your views on the current financial management system, in particular the Discharge process, in ensuring EU budget funds are properly spent and audited?

Nothing to add.

6 What are the advantages and disadvantages of having some expenditure, including to provide flexibility, held 'off-budget'?

Greater flexibility could be an advantage in times of economic crisis, facilitating a more rapid response; however, it could be difficult to determine what rules should apply (and who should decide) how such funds might be deployed.

7 What are your views on the future structure of the EU budget and should the system change to reflect developments in the Euro Area? Should there be differentiated systems between Euro Area and non-Euro Area Member States, for example to allow fiscal transfers?

It is difficult to envisage that the structure of the budget would change significantly in future given the drivers underpinning agreement on the budget – net balances and *juste retour*, coupled with national vetoes. It seems likely that the budget will decline in importance as a motor of integration as well as falling further in real terms. It remains to be seen how the proposals for a euro area fiscal capacity will develop.

General value of spend

8 In your view, is the EU budget focussed on areas of EU added value in expenditure?

This depends on how 'value added' is defined - and how it is perceived will differ between countries - but in general it can be argued that the value-added is limited, for the reasons outlined in 1 above. Increasingly, there has been an emphasis on 'value-added' and the perceived need to focus resources on areas that can deliver growth and jobs, support for innovation and R&D and the capacity to produce European level public goods. In the run-up to the current budget proposals this was emphasised heavily by a number of Member States, notably the net contributors. However, net contributors also staunchly defend Cohesion policy receipts and it doubtful whether the flow of funds

to regions of prosperous Member States from national budgets through the complex financial circuitry of EU finances is capable of delivering much value added.

9 What modes of expenditure (e.g. bid-based expenditure, automated expenditure, loans, grants) in the budget represent the most effective use of EU funds?

There is no single answer to this; different modes of expenditure are suited to different circumstances both in policy terms and in relation to the economic cycle.

10 What is the right level for the EU budget?

This is entirely contingent on decisions about the purpose of the budget.

11 What are the arguments for and against increasing or decreasing the degree of national flexibility in spending money allocated to Member States under one part of the EU budget in other parts of the budget?

As noted above, increased flexibility can facilitate responses to changing circumstances. However, there are risks in terms of planning and predictability. There are also questions around the extent of the flexibility and whether this might undermine the original purpose of the funding. Moreover, the same rule on flexibility would need to apply to all Member States, which might render the prospect of increased flexibility less attractive.

The resource system

12 What are your views on the current system whereby the EU budget is resourced on the basis that Member States contribute in relation to their income, with corrections where necessary?

The current system based on GNI is reasonable in terms of fairness and efficiency. However, the corrections on contributions are difficult to justify; 'corrections' should, arguably, be part of the expenditure side of the balance sheet, not an adjustment of contributions. However, UK defence of the rebate is one of several elements that impede a wholesale reform of the EU budget.

13 Do you have any other points to raise relating to the EU budget system, not covered by the questions above?