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Stiftung
Wissenschaft und
Politik

German Institute
for International and
Security Affairs

More Money for Europe

Agreement on a new EU Financial Framework for 2007–2013

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By reaching a political consensus on a new Financial Framework in mid-December 2005, at best the European Union can be said to have finally struck a deal and demonstrated its ability to act. However, the compromise reached by the European heads of state and government by no means marks the end of the marathon negotiations that began way back in February 2004. Indeed, first the Council of Ministers must haggle with the European Parliament over the new Financial Framework; then the 25 EU Member States' respective national parliaments will have to ratify a new Own Resources Decision. Moreover, the fact that the European Parliament so flatly rejected the compromise reached at the Brussels Summit is a clear indication of just how difficult this final phase of the process will turn out to be.

After the failure of the Luxembourg EU Presidency to broker an agreement in June 2005, for a long time it looked as though the UK Presidency would follow suit, especially since initially the United Kingdom—amongst other things under the shock of the London terror attacks—made no major effort to pick up the negotiations where its Luxembourg predecessor had left off. Indeed, the drive and desire for change expressed in Tony Blair's brilliant speech in the European Parliament on 23 June 2005, appeared to have fizzled out rather quickly.

Consequently, it was only on 5 December that the UK Presidency submitted a new negotiating paper, to which it made minimal changes just before the Summit, in response to fierce criticism. In its new proposal, the British government set about freshly delimiting the leeway for reaching an agreement, and reduced the scope for negotiation to the difference between the last Luxembourg proposal of 17 June and its own subsequent version dating from 14 December 2005 (a total of roughly €133.7 billion). Compensation and minor amendments were primarily sought with reference to a list of special measures and technical and/or administrative adjustments.

Although a compromise was ultimately reached on the basis of the UK proposal on 17 December, this is at best cause for relief, rather than joy.

Political Assessment of the Summit

The European Council's present compromise prompts one negative and two positive conclusions:

1. The negative conclusion is that the new Financial Framework largely perpetuates the familiar European status quo. Both the contents of the negotiations and the negotiating process itself followed well-trodden paths. The respective positions taken up by individual Member States in the financial negotiations were all too clearly geared towards the so-called 'net balance'. Combined with the requirement of unanimity, this preoccupation with net balance inevitably leads to a frequently criticised bazaar mentality in the European Council and to haggling over relatively modest amounts, by comparison with the sums under discussion in national budgets. This policy of focussing on net balance undermines efforts to achieve European added value that would potentially benefit all.

At the same time, this manner of proceeding leads to both the disproportionate stiffening of agreed compromises and the ossification of previously introduced measures. The European Council simply continued to resort to special measures that were tied to particular conditions or only approved for a limited period. For instance, Member States whose regions no longer met the criteria for support from the European structural funds managed to make sure that such aid would only be phased out over a very protracted period. Consequently, even thinly populated regions of Sweden, Finland and Austria, for which a special support programme was set up in 1994 in line with those countries' treaty of accession, will continue to receive funds from the EU budget. In fact, in future they even stand to receive aid on top of the structural funds already set aside for the Member States in question. In 1999 a special payment to the United Kingdom and Ireland was authorised to support the peace process in Northern Ireland, and the present compromise also provides for special assistance of this ilk for Northern Ireland.

There are two dangers in perpetuating what were originally introduced as 'special' measures and allowing the clear spread of such non-standard aid schemes:

a. Firstly, the EU Financial Framework will only become more complicated and even less transparent, and the EU's support policy will end up being negotiated more blatantly than before on the basis of fiscal criteria.
b. The misuse of EU support programmes to 'fine-tune national net balances not only softens objective criteria for support, but also relativises common European standards. Eligibility for funding thus becomes a political bargaining chip and runs the risk of becoming discretionary, and the exception threatens to become the rule.

2. On the positive side, by reaching its agreement, the European Council managed to conclude an arduous, conflict-ridden negotiating procedure. The compromise not only lays a secure basis for planning and financing further European legislative activity, but also provides the stability needed to continue the process of political integration. Not for nothing, after the European Council reached agreement on the Financial Framework, did the issue of the ratification of the Constitutional Treaty once again occupy centre stage in European policy. However, it remains extremely uncertain whether reaching agreement on the Financial Framework will suffice to inject fresh momentum into attempts to resolve outstanding issues (such as pressing ahead with the ratification of the Constitutional Treaty and adopting the EU Services Directive).

3. Some analysts heralded the new federal government's successful negotiating strategy as 'the return of Germany'. And even if this headline exaggerates the role played by Germany and its first lady chancellor, the fact nevertheless remains that the country's diplomacy at the Summit effectively expanded its room for

manoeuvre within the EU. In addition to the clearly close cooperation with France, as reflected in the outcome of the negotiations, Germany also intensified its talks with the United Kingdom and the smaller EU Member States. In this respect, two German initiatives pointed the way ahead:

a. The push to raise the restrictive and loudly criticised British proposal by around €13.2 billion opened up new leeway for negotiation, especially with respect to effecting additional special payments to small EU Member States.
b. By desisting from the €100 million set aside for its eastern *Länder* and allowing Poland to benefit instead, Germany highlighted its readiness to put the attainment of an overall compromise ahead of its own national interests. This underscored Germany's strategy in the negotiations not just with words, but also with a willingness to compromise that was clear for all its EU partners to see. The decision to do so cannot merely be interpreted as giving the new government in Poland, which is tainted with an antipathy towards Germany, a certain 'benefit of the doubt', but should also be viewed as both a political gesture to all other small EU Member States and firm proof that the new German government is prepared to shoulder its fair share of the overall burden.

Faced with the restrictive British negotiating strategy and the equally unbending position taken up by France in its refusal to modify the compromise on agriculture reached in October 2002, Germany almost inevitably grew into the role of fair mediator between conflicting interests. The German delegation was evidently skilful in its exploitation of this role, managing to reconcile existing differences without relinquishing any previously made commitments. In the long run this policy could lead to Germany regaining its function as a centrally placed arbitrator between East and West, which is surely significant, given the fact that next year Germany faces the prospect of an EU Presidency that can be expected to prove problematic.

Cornerstones of the New Financial Framework

The hard-won compromise can be broken down into six key constituent parts:

1. Total volume of appropriations for commitments: The total amount agreed on for the seven years of the Financial Framework was €862.363 billion, or 1.045% of the EU's gross national income (GNI). This made the resulting sum around €15.6 billion higher than the original British proposal of €846.754 billion and €9.25 billion less than the failed Luxembourg proposal of €871.614 billion. Accordingly, the European Council lopped over €162 billion off the total of €1,025.035 billion initially proposed by the European Commission in February 2004. In its resolution of 8 June 2005, the European Parliament had also made it clear that it wanted to see more money become available (see Table 1 on p. 5).

As a result, the new Financial Framework provides for a faint rise in overall expenditure averaging 0.7% a year, on top of an automatic adjustment to the rate of inflation.

2. Allocation of funds: Out of the total of around €862 billion, approximately €307 billion are spent on the European structural funds and some €293 billion are earmarked for market-related agricultural expenditure and direct payments made to farmers. This leaves about 70% of the budget for the Common Agricultural Policy and European cohesion policy. A further €70 billion are set aside for the development of rural areas and environmental policy; but €33 billion of this total is reserved for the 10 new Member States and Bulgaria and Romania. All in all, the agricultural budget totals approximately €363 billion.

The European structural funds are divided into two roughly equal sums between least-developed regions in the old and new EU Member States. And although the amount earmarked for the new Member States is well below the total originally called for by the Commission, in future the co-financing share that the poorer Member States will have to contribute out of their national budgets will be reduced by 10 percentage points. Furthermore, private investment costs and even VAT will be included in this co-financing share. Additional relief is provided by a one-year extension from two to three years of the period during which the funds centrally allocated in Brussels can be claimed. These technical adjustments should go much further towards meeting the needs of strained national budgets and frequently overstretched fund managers in the new Member States than a simple increase in the overall funds in question.

The clearest increase over the entire period is under heading 3a "Freedom, security and justice." Here, the funds provided for the common asylum and immigration policy, the protection of the EU's external border and joint measures designed to combat illegal immigration, organised crime and terrorism are to more than double, albeit rising from the comparatively low figure of €600 million in 2007 to €1.390 billion in 2013.

A substantial rise of over 50%, with a fixed annual increase in real terms of 7.5% compared with 2006, was agreed for heading 1a "Competitiveness for growth and employment," which primarily serves to finance trans-European networks, EU programmes in education and training, research and development and measures ensuing from the Social Policy Agenda 2005–2010 and European employment policy. However, contrary to the original British demand for a significant increase in EU support for research and development, only the appropriations suggested by the Luxembourg EU Presidency back in June 2005 were left untouched. Another proposal that was retained entailed using an additional financing facility provided by the European Investment Bank, with the risk shared by the EU and the bank, to boost the volume of funding by up to €10 billion. This money is to be used to promote private-sector research and development. However, it is hard to see why the special funds (€1,24 billion) needed to close down two unsafe nuclear power stations—Ignalina in Lithuania and Bohunice in Slovakia—should be financed out of this budget heading.

In spite of Germany's reservations, the European Council opted to set up a new 'Globalisation Fund' of €500 million per annum, in line with the suggestion made by Commission President Barroso. The resources in this fund are to be spent, amongst other things, on retraining employees in the event of delocalisation or closures by major companies. Nonetheless, no additional funds will be forthcoming for this fund, since its purpose is also covered by the new PROGRESS programme, which is part of the EU's employment and social policy. Instead, the fund will be fed largely out of resources not used by other programmes.

The funds set aside for the EU's Common Foreign and Security Policy are to go up by 4% per annum. In other words, the EU estimates that it will need to spend roughly the same amount of money on administration as on neighbourhood policy, pre-accession assistance and the new stability and development funds.

3. Special measures for individual Member States: A prominent feature of the new Financial Framework is a marked increase in the number of 'special measures' for individual Member States. Whereas Agenda 2000—the current Financial Framework—contained 13 special measures worth a total of €5.265 billion, the new Financial Framework will contain a total of 18 measures worth well over €10 billion. The associated provisions concern items ranging from special payments made to individual regions like Ceuta and Melilla, Corsica, Northern Ireland, Prague, the poorest regions in eastern Poland, Ger-

Table 1
Comparison of proposals for the Financial Framework 2007–2013 (in € billions)

	European Commission (10/2/2004)	*European Parliament (8/6/2005)*	*Luxembourg Proposal (17/6/2005)*	*British Proposal (12/12/2005)*	*Negotiated result (17/12/2005)*
1a Competitiveness (Lisbon Strategy)	132.755	120.563	72.010	72.010	72.120
1b Cohesion (structural funds)	338.710	338.472	308.558	298.989	307.619
2 Preservation and management of natural resources	404.655	396.248	377.801	367.294	371.245
including market-related expenditure and direct payments in the agricultural sector	301.074	293.105	295.103	293.105	293.105
3 Citizenship, freedom, security and justice	24.705	19.437	11.000	10.270	10.270
4 The EU as a global partner	95.350	70.697	50.010	50.010	50.010
5 Administration	28.620	28.620	50.300	49.300	50.300
6 Compensation (Bulgaria, Romania)	240	800	800	800	800
Commitment appropriations	1,025.035	974.837	943.064	809.319	862.364
as a percentage of GNI	1.26	1.18	1.06	1.03	1.045

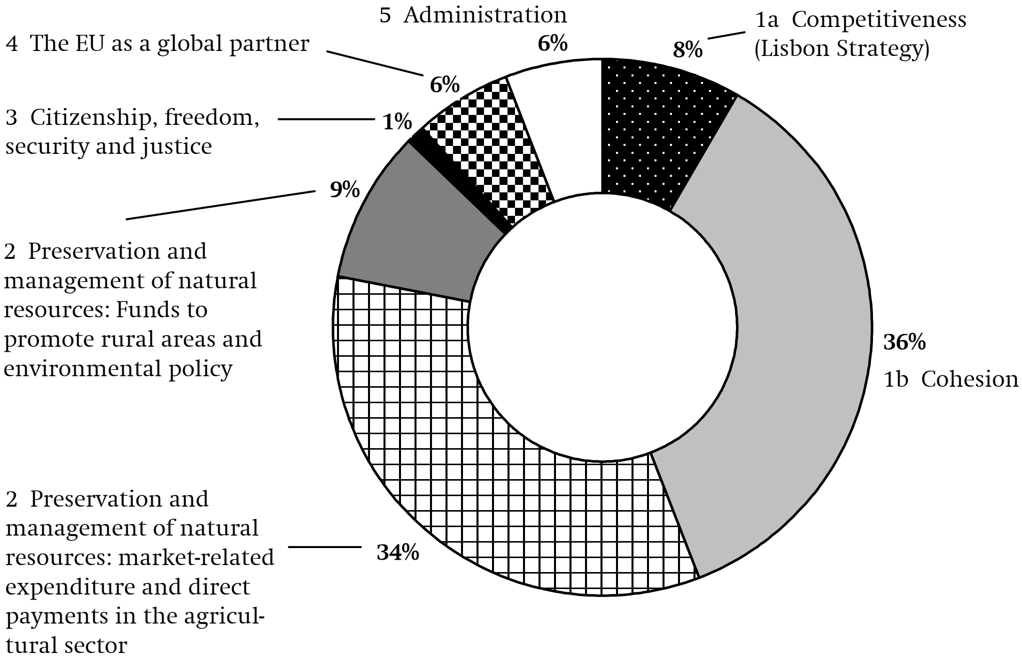
many's new federal states, Bavaria and Austria's border regions to special measures for dividing up the funds of the new financial instrument EAFRD (European Agricultural Fund for Rural Development) between a few Member States in Western Europe. It is difficult to calculate the precise volume of these special measures, because in many cases instead of fixing absolute figures, special target amounts were agreed (e.g. per capita aid or the inclusion of individual regions in special transitional arrangements). Nonetheless, the countries standing to gain the most from such exceptional measures will be Spain, with special payments totalling at least €2.1 billion, Italy (€1.9 billion) and Poland (€1.2 billion).

At the same time, various special measures were introduced on the income side of the Financial Framework to reduce the negative balances of the so-called 'net contributors' Austria, Germany, the Netherlands and Sweden. In this way Sweden and the Netherlands managed to negotiate substantial reductions in their gross contributions.

4. The British rebate: Whereas the initial British proposal suggested only a gradual reduction in the British rebate totalling €8 billion and limited to the period 2007–2013, in the end it was agreed that the rebate would be cut by a maximum of €10.5 billion throughout its duration and that this reduction will also extend beyond the year 2013. In this way the United Kingdom will assume a greater share of the additional burden on EU structural policy arising from the EU's eastward enlargement, but will continue to benefit from its full rebate on agricultural expenditure even now that the EU has ten new Member States.

5. Germany's net balance: Immediately after the EU Summit, the compromise was criticised by the opposition parties in the lower house of Germany's parliament, the Bundestag, because it would mean a very

Figure 1
Funds allocated with the Financial Framework



sharp rise in Germany's contribution and a corresponding deterioration of the country's net balance. In response, the federal government stressed that the agreement reached would represent a lesser burden on the German budget than initially calculated. Nonetheless, according to the federal government's initial calculations the country's net balance will rise by some €2 billion, compared with 2006, to average approximately €10.4 billion per annum, and Germany will remain the Union's biggest net contributor, shelling out 0.43% of its GNI, ahead of Italy, France and Sweden, which each pay 0.37% of their national GNI. Thus, Germany will finance roughly 19% of the Financial Framework on average, slightly less than what it has been paying up to now (over 20%). Moreover, having received EU structural funds totalling around €18 billion over the period 2000 to 2006, under the new Financial Framework for 2007 to 2014, the eastern *Länder* will only receive around €13.3 billion, equivalent to a reduction of about 26%.

In future, Poland will be the biggest net recipient, receiving approximately €55 billion.

6. Revision clause: To meet demands made by a number of Member States for a comprehensive overview of the EU's financial system (Sweden had backed the United Kingdom's call for such a fundamental reform), the compromise contains a special 'rendezvous clause'. Under this clause, in 2009 the heads of state and government intend to go ahead with a comprehensive 're-evaluation of the Financial Framework'. This process will cover items on both the income and expenditure sides of the EU budget, with the Commission being requested to conduct a full, far-reaching review by 2008–2009. Importantly, the rendezvous clause explicitly mentions both the Common Agricultural Policy and the British rebate. As Tony Blair stressed in his final speech to the European Parliament as president-in-office of the

Council on 20 December 2005, linking these two key areas of reform on the income and expenditure side could pave the way for a comprehensive, lasting reform of the structures of the EU's financial system. At least, according to European Commission President Barroso, the European executive will include all budget categories and policies in its review and publish a white paper in 2008. Without expressly using the term 'EU tax' Barroso called for an autonomous source of income for the EU, the aim being to make the Union less dependent in future on difficult budget negotiations.

For all that, the wording of the revision clause is extremely vague, not naming any key points or setting any objectives for the planned in-depth overhaul of the EU Financial Framework. The vagueness of the clause and the fact that the new Financial Framework will cover the period extending up to 2013 means that there are now two conceivable, but incompatible scenarios:

Scenario 1: The 2009 revision will be considered by the Member States as a non-binding preliminary phase to the actual negotiations on the next-but-one Financial Framework (from 2014 to 2020) that will start in 2011. In the absence of any imposed deadlines or objective pressure to reach agreement, the Member States will negotiate without any true ambition to reform, adopting maximum positions serving their national interests, and will discuss the European Commission's white paper in unimportant 'basic negotiations'. Any alteration of the status quo will be measured against the impact on the national net balance.

Scenario 2: The Commission will use the open wording of the clause to engage in broad public discourse about reform, focussing primarily on the European added value of common policies and their adequate funding. The Commission's partners in the ensuing debate would be the European Parliament, a few reform-minded Member States and their national parliaments. However, following the near collapse of the last round of negotiations, such a 'reform coalition' would have to keep alive the currently palpable willingness to embrace reform until the year 2009, to prevent any reversion to 'familiar behaviour'.

The Final Phase of the Negotiations

The European Council's compromise is the culmination, but by no means the actual end of the negotiation process on the EU's Financial Framework. Instead, the present agreement reached by the heads of state and government, which is only politically binding, will have to be made legally binding as well. To this end three legal instruments will have to be negotiated:

1. An *Interinstitutional Agreement (IIA)* between the European Parliament, the Council of Ministers and the European Commission on the legal consolidation of the Financial Perspective. The term 'Financial Perspective' is nonexistent in European contract law. Indeed, Article 272 of the EU Treaty merely details the procedure for the adoption of the EU's annual budgets by the Council of Ministers and European Parliament. Hence the new Financial Perspective requires the special form of an IIA, as recognised under EU law, so that the European Parliament is also bound by the provisions and limits of the Financial Framework in its capacity as an equal partner among the EU budgetary authorities.

2. The adoption of more than *30 legal texts*, forming the basis of spending programmes in the various areas of policy and mostly adopted by way of the co-decision procedure involving the Council of Ministers and Parliament. Almost 90% of all spending programmes will expire at the end of 2006 and will require a fresh legal basis so that they can continue in 2007.

3. A new *Own Resources Decision* incorporating amongst other things the changes in the British rebate. This decision will need to be ratified by the respective national parliaments.

This will open up a new arena for negotiations, characterised by the direct inclusion of the European Parliament in the negotiating process . MEPs will not only be able to make a few direct demands of their own, but also call for changes in the political agreement reached by the European Council. The European Parliament's blunt rejection of the outcome of the negotiations on 17 December and experience from previous negotiations suggest that MEPs will not be prepared to back all compromises reached by the European Council without discussion.

In June 2005 the European Parliament already summed up its demands in a resolution and drew up its own financial table, arriving at a figure of €975 billion, well above the €862 billion resulting from the negotiations. In addition, Parliament sought to highlight other political issues than had been agreed. For instance, it proposed that more funds should be set aside for attaining the Lisbon objectives, for the European justice and home affairs policy and the Common Foreign and Security Policy, and suggested that less money should be earmarked for direct payments to farmers. In fact, here Parliament had even proposed the adoption of co-financing.

Lastly, on 1 December 2005 MEPs formulated four 'non-negotiable' positions:

- To be able to respond appropriately to 'ongoing changes' in the Financial Framework, the European Parliament is calling for a revision mechanism that would enable a comprehensive review and alteration of the then current Financial Frameworks for 2007 to 2013, in which Parliament would be entitled to take part on an equal footing with the Council of Ministers.
- So-called flexibility instruments should be markedly increased. Parliament wants to see a new multi-annual instrument of this kind, worth roughly 0.03% of the EU's GNI, i.e. approximately €20 billion. This sum should be provided outside the Financial Framework and be accessible in the event of natural catastrophes, international crises and economic upheavals by virtue of a joint decision taken by the Council and Parliament.
- A review of the Financial Regulation and thus an improvement in the quality and efficiency of the EU's budget implementation and spending.
- Introduction of the co-decision procedure in new EU programmes in the Common Foreign and Security Policy.

MEPs have thus made it abundantly clear that they cannot approve a new IIA if these demands are not taken on board, in which case the only conceivable way out would entail falling back on the procedures set out in Article 272 of the EU Treaty, namely having annual budgets negotiated between Parliament and the Council. However, such a 'solution' would mean clearly less planning security with respect to the distribution of EU expenditure.

Whilst the Member States are very keen not to re-open the fragile compromise package agreed by the heads of state and government, MEPs are intent on pressing their claims in Parliament's negotiations with the Council. At the same time, neither side would have anything to gain by seeing these talks fail, for that might not only delay the next funding periods, but also result in fewer funds being awarded.

The Austrian EU Presidency plans to conclude the negotiations with the European Parliament, due to start on 23 January, by March, so that the decree-laws for the respective spending programmes can subsequently be swiftly adopted.

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ISSN 1861-1761