

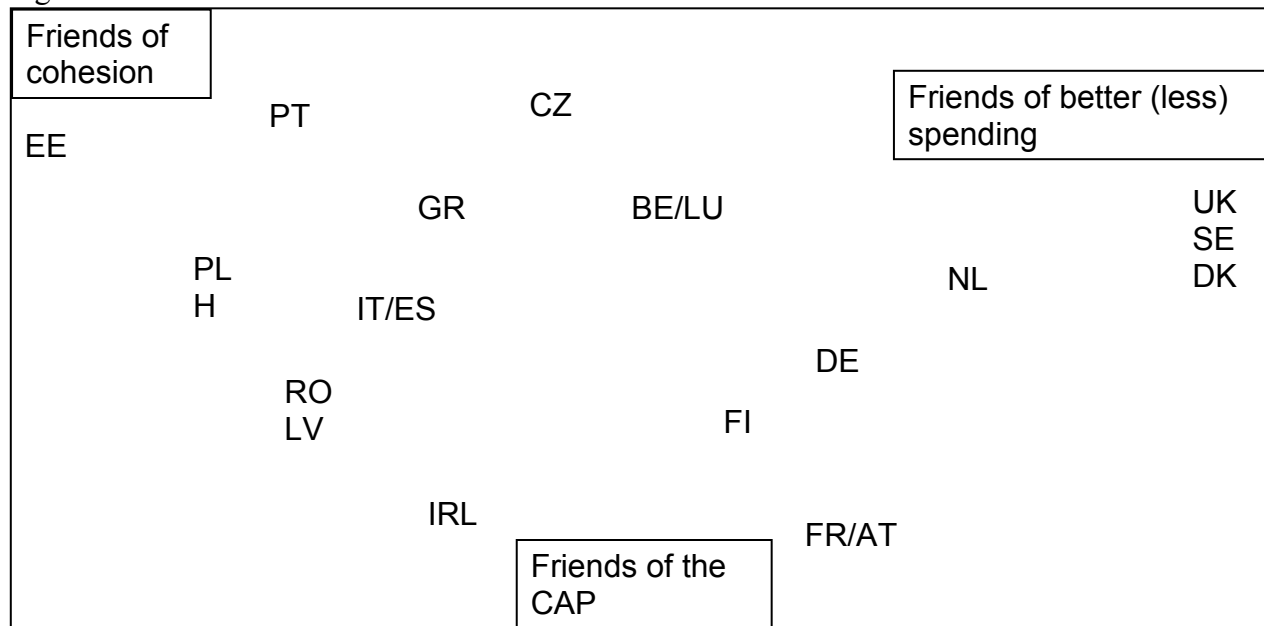
## MFF 2014-2020: less money, less Europe? Prospects, interests, explanations

On 25 November 2013, the Institute of World Economics, Centre for Economic and Regional Studies of the Hungarian Academy of Sciences (IWE MTA KRTK) hosted an international workshop about the European Union's next Multiannual Financial Framework (hereafter MFF). The professional meeting took place six days after the budgetary framework of 2014-2020 had been confirmed by the European Parliament. This vote had to be followed by another formal vote in the Council (effectuated on 2 December 2013) enabling this seven-year program of nearly EUR 1 trillion to be launched soon.

In his opening remarks, **Miklós Somai**, senior research fellow of IWE MTA KRTK and co-ordinator of the workshop, gave a brief overview of the new MFF, its negotiation process, and compared the outgoing (2007-2013) and the new (2014-2020) MFF in terms of their main figures. He highlighted that resources in real terms would grow most under those headings (competitiveness) and sub-headings (research) where the new member states have less chances to draw on EU funds (at least based on experiences from the period of 2007-2011). At the same time, those expenditure items were cut the deepest (agricultural and cohesion policies) where these countries were more successful in obtaining community assistance. Based on the above, the adopted changes to the MFF system do not seem to favour the new and/or less developed member states of the EU.

The keynote speech of the meeting was delivered by **Johan Ureel**, head of unit at the European Commission's Directorate General for the budget. Having been involved in financial programming, and later in the whole negotiating process, the speaker provided detailed information about the main stages of the bargaining process, and the member states' interests regarding the future financing of the different common policies (see Figure 1).

Figure 1

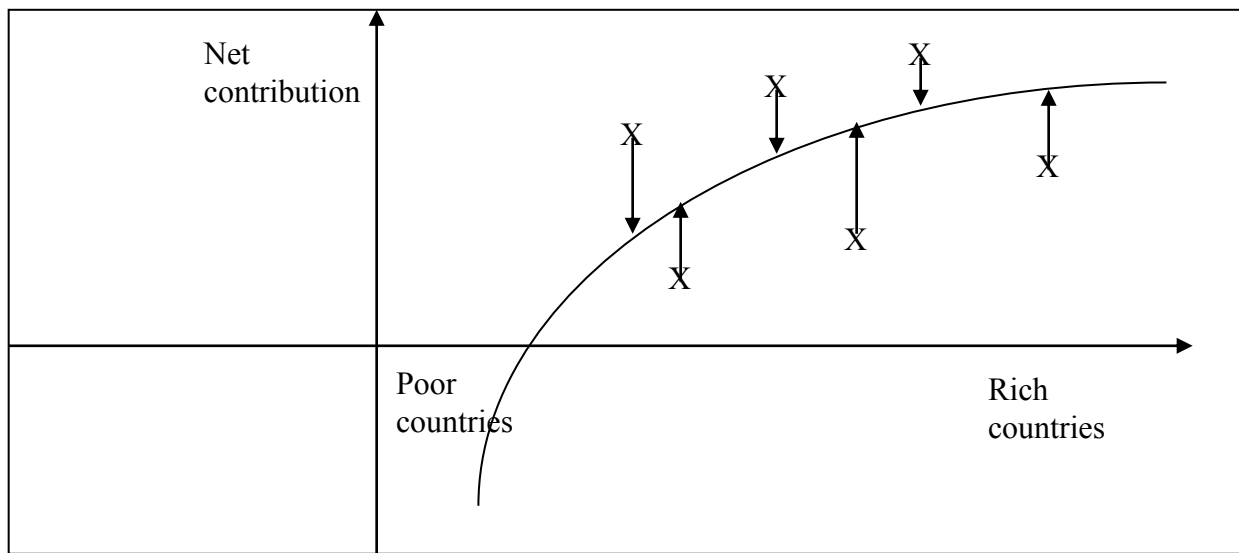


In its original proposal of 29 June 2011, the Commission suggested a freezing of the spending ceiling (adjusted with 2% of annual inflation), which idea proved to be untenable due to the

inflexible attitude of net contributors, especially that of the United Kingdom. To reach an agreement was not an easy business as the member states were divided into three groups of interest: that of *Friends of better* (in fact: less) *spending* arguing that the money available in EU funds had never been fully utilised, hence the revenue ceiling must be set at a lower level; that of *Friends of the common agricultural policy* (CAP) led by France, trying to preserve the essence of the CAP as well as its financial envelop; and finally that of *Friends of the cohesion policy* (the biggest of the groups) rejecting the idea of curtailing the resources earmarked for development.

The Commission intended to reform the Own Resources System and proposed such new types of resources as the Financial Transaction Tax or the new VAT resource coupled with reformed correction mechanisms – but the member states rejected all these initiatives. Even more interesting is another proposal of the Commission (turned down too) which aimed to display member states’ net contribution to the common budget by using a logarithmic function and would have adjusted any deviation in member states’ net position by a standardised correction mechanism (see Figure 2). Naturally, a debate could have been opened on how to calculate the curb of the function, but it failed before it started due to member states’ resistance. According to the speaker, there could be two reasons for this resistance: first, it was perhaps too late (in autumn 2011) for the Commission to come out with such a plan; second, such a normative system would have precluded any exceptions and bonuses, i.e. it would have been too transparent and would have deprived politicians of the possibility to bargain special arrangements for their countries.

Figure 2



X = initial net position ↓ ↑ = correction

The early negotiating process was treated cautiously by both the Polish and the Danish presidency. At this stage, the indication of concrete figures was avoided while over one hundred questions for discussion had been gathered in the common “negotiating box”. In the second half of 2012, under the Cypriot presidency the president of the European Council Herman Van Rompuy tried to clarify the interests, positions and red lines of each member state by consulting with their representatives individually. The efforts to harmonise all interests bore fruit in the beginning of February 2013, when the heads of state and government were able to adopt the MFF for 2014-2020. Commitment appropriations were set at EUR 960 billion while payment appropriations at 908.4 billion, which represent 1.00% and 0.95% of the Union’s GNI respectively (as opposed to 1.045% and 0.99% in the 2007-2013 MFF).

Even though the European Parliament (EP) voiced sharp criticism in its resolution of March 2013 – inter alia complaining that by disregarding the spirit of the Lisbon Treaty the decision-makers did not involve the EP sufficiently and tended to ignore its opinion – finally a compromise was met in June and thus the EP, the Council and the Commission could conclude a political agreement on the MFF. (Consequently the approval on 19 November was a simple formality.) In addition to the approved package, the EP achieved that non-executed payment appropriations can, under certain circumstances, be moved to next year; that in 2016 a mid-term review of the MFF should be undertaken; and also, that a high-level working group dealing with the revision of own resources should be set up.

By concluding his contribution and also referring to the question in the title of the workshop, the speaker highlighted the fact that in none of the previous budgetary frameworks was all the available money spent. This is equally true for the MFF of 2007-2013. Consequently, and taking into account the possibility for greater payment flexibility between financial years achieved by the EP, it is by no means certain that in the upcoming MFF less money could effectively be used than in the previous one. Now, as far as the share of the budget in the EU's GNI is concerned, it also depends on the denominator, namely the gross national income of the 28. So, in case of a persisting near-stagnation of the European economy, the spending measured in GNI will not decline either.

The next speaker of the conference was **Adam Ambroziak**, associate professor of the Warsaw School of Economics. He started out by emphasising that Poland attached great importance to belonging to the presidency trio that had to tackle the MFF. At the same time, not having to deal with concrete figures was a relief for the Polish presidency. The finally adopted MFF is perceived in Poland as a win-win situation. As the biggest net beneficiary, the country will be eligible for EUR 106 billion in the upcoming seven years which exceeds its current (2007-2013) entitlement by some EUR 4 billion. This can be explained by the fact that – similarly to all countries that joined in 2004 (EU-10) – the new beneficiaries of both the common agricultural policy and the cohesion policy underwent a kind of a phasing in period which means that their accession to these policies was a gradual process. Thus, while the financial envelop covering these two policy areas will in real terms decrease from the level reached in 2013, the EU-10 group of countries as well as Romania and Bulgaria (due to the completion of their phasing in periods) will on the whole be able to benefit from more support than in the previous financial framework.

The Slovenian position on the new MFF was exposed by **Rok Tomsic**, minister plenipotentiary at the Embassy of Slovenia to Budapest. During the negotiations, the main aim of Ljubljana was to maintain its net beneficiary position, and this objective was fully met. Another key goal was to preserve the amounts of money available for infrastructure and rural development as well as to introduce the so-called regional safety net under cohesion policy. The latter guarantees 60% of initial assistance in case the eligibility category of a given region would alter. Even though the country managed, despite the crisis, to catch up in the last seven years (which is especially true for Western Slovenia to become a competitiveness region under the next MFF) the nation may get EUR 1.6 billion annually, which is just slightly lower than their 2007-2013 level. At the same time, the Slovenian net position in terms of gross domestic product is set to improve from a net surplus of 0.87% to over 1% of GDP. This outcome makes the country satisfied with the upcoming MFF.

The Slovenian case was followed by the Hungarian analysis, presented by **Géza Hetényi**, head of the EU Economic Policy Department of the Ministry of Foreign Affairs. Regarding the size of the

multiannual budget, the country has always had a bottom-up approach, namely that the financial means should be tailored to commonly determined goals. Unfortunately the opposite happened: the approach focusing first on the total sum prevailed. As to the expenditure structure, Hungary was interested in keeping both CAP and cohesion spending as high as possible. Given the fact that the Friends of the CAP group was supported by some strong member states, Hungary could concentrate its efforts on defending cohesion policy assistance. The big challenge for Hungary is the new GDP cap for beneficiaries that was cut back to 2.35%. This is further aggravated by the GDP projection methodology of the EU according to which the Hungarian growth rate would be the lowest in the Union in the next seven years. In the end, as this problem was shared by the Baltic States too (given these four countries' extremely poor economic performance in the reference years of 2008-2010) a special key was adopted for them: they can use cohesion financing up to 2.59% of their GDP. A further problem for Hungary – shared by other member states too – is that the region of Central Hungary comprises the highly developed capital city as well as its lagging surroundings. The whole area counts as a competitiveness region, thus the less developed parts will be eligible in 2014-2020 for much less assistance than what they received in 2007-2013. At the same time, Hungary welcomed that the co-financing rate for the poorest regions remains 85%, that VAT-eligibility will be possible, and also that the so-called n+2 rule was changed to n+3 enabling a one-year longer financial implementation of a given project under cohesion policy.

In the next part of the conference the position of the three biggest net payers was explained. **András Hettyei**, research fellow of the Hungarian Institute of International Affairs spoke about the EU budget's greatest net contributor. Germany was founder and informal leader of the group called Friends of better spending. This role was fully consistent with the country's general EU policy characterised by austerity, fiscal consolidation and structural reforms advocated since the outbreak of the euro crisis. The German position was however also influenced by the fact that the country is a big beneficiary of both cohesion and agricultural assistance, thus the moderation of spending cuts in these areas was also in their interest. In the end of the day, Berlin could be satisfied with the final MFF agreement as total expenditure has been cut compared to the previous cycle. Although Germany will get 40% less of cohesion money, at the same time Berlin will be able to retain its corrections and will also benefit from a one-off EUR 700 million support to be spent on development of the Eastern regions of the country.

According to **Anita Szűcs**, assistant professor at the Corvinus University of Budapest, France too – as the second biggest net contributor to the EU budget – aimed at lowering the spending ceiling. The primary reason behind this attitude was the protracted sluggishness of the country's economy. Actually, Germany and France shared many fundamental negotiating points, such as freezing expenditures at 1% of EU GNI, rejecting the reform of correction mechanisms (with regard to the interests of the UK – their main ally in the previous issue) as well as keeping the level of direct payments as high as possible. The political shift from right to left just in the middle of the MFF talks did not bring about any substantial change in the French approach. Maybe two areas deserve attention from this perspective. The first was the weakening interest of France in curtailing cohesion assistance given the overwhelming majority of Socialists-ruled regions whose claims for EU Funds was difficult to resist. Secondly, the initial opposition against the CAP's "greening" was also fading as the new French government has members from environmentalists too. All in all, the country's net budget balance will deteriorate by EUR 15 billion in the whole seven-year period of the 2014-2020 MFF. Nevertheless, Paris hopes that the new financial framework, that dedicates more money than ever for research and infrastructure upgrading, will contribute to growth and boost employment without overburdening the national budget.

Following the presentations on Germany and France, **Miklós Somai** gave a brief overview of the UK's approach to the new MFF. Her Majesty's government literally celebrated the agreement on the next MFF, as the first budget in EU history which would spend less than 1% of Europe's GNI. Since in the previous MFF negotiations the (Labour) government had already sacrificed on the altar of Eastern enlargement as much as EUR 10.5 billion of the *rebate*, there were, according to the current prime minister David Cameron, only two sensible goals the British negotiating team could set for itself. First, to get the overall budget down and second, to protect what was left of the *rebate*. In order to achieve their first goal, the British found good allies in the Germans, the Swedish, the Dutch and the Danes. In the case of the *rebate*, as its change requires unanimity in the Council, the Brits were deemed to succeed. In Cameron's opinion, the agreed payment limit of EUR 908.4 billion is EUR 80 billion lower than the Commission's original proposal; EUR 35 billion lower than the previous MFF deal; and EUR 60 billion lower than the emergency arrangement that would have entered into force in the absence of a deal. The latter would have meant that the existing ceiling of 2013 (the last year of the current MFF) would have automatically been rolled forward. From the British point of view, further good news is the growing share of expenditure targeted towards research and development, connecting the European infrastructural networks, and other pro-growth investments. The British think their universities are well placed to win research contracts from the European budget. They do, however, feel disappointing that administrative costs still amount to around 6% of the total.

After the first panel which was dedicated to the member states' approach (and following a short coffee-break) the conference program went on with the second panel focusing on a thematic approach. As the first of the panellists, **Gergely Papp**, professional deputy director of the National Agricultural Chamber of Hungary, dealt with the financial and regulatory aspects of the common agricultural policy (CAP) during the next seven-year period. He explained that the 2014-2020 MFF had only answered the question "how much money could be spent" on the CAP. At the same time, the new CAP reform, agreed upon in parallel with the MFF deal, provides detailed information about "how the money can be spent". According to the speaker, much can be said about the post-2013 CAP, but not that it will be common. In practice, there will be 28 different agricultural policies, thanks to the new regulation that makes the whole system largely flexible and renders several of its main elements optional. Regarding the direct payments, the end-date for the simpler, flat-rate Single Area Payment Scheme (SAPS), still in use in most of the new member states, will be extended until 2020; the share of "coupled" payments, i.e. linked to a specific product, may reach as high as up to 15% of the national envelop; and in case of general market disturbances the Commission will, for all sectors, be authorised to take emergency measures. Further flexibilities and options involve the possibility to direct subsidies towards young farmers, small farms, less favoured areas and areas with natural constraints, and also the possibility of transferring funds between the two pillars of the CAP (i.e. between direct payments and the rural development envelop). Taking into account the enlarged set of policy instruments available under the new CAP as well as its "*à la carte*" character, for smaller member states it will be better not to be in a hurry to elaborate their own policy mix; instead, they better wait for their neighbours and/or their biggest client country to decide first, lest a hasty step might hopelessly disadvantage their operators in one or more sectors of the agri-food chain.

The analysis on the future of the CAP was followed by an evaluation of cohesion policy. **Ákos Kengyel**, associate professor at the Corvinus University of Budapest highlighted that despite a smaller financial envelop, convergence of development levels in the Union does remain a key priority in the next seven years. At the same time, the idea to link the available amount of money to the Europe 2020 strategy (broken down into 11 objectives) signals the lack of concentration of resources. The economic, social and territorial cohesion of all EU regions and countries would

boost the competitiveness of the whole of the Union, therefore this type of assistance should not be seen as welfare transfers but rather as development investments. Even though the net payers managed to cut back the relevant budget heading, the losses can be offset by successful absorption. This however requires an adequate institutional set up, a competent staff for programme design and application, and there is also need for appropriate communication towards the potential recipients. But unfortunately, several countries struggle with absorption problems due to co-financing challenges, exaggerated bureaucracy and lack of well-trained personnel.

As the last speaker of the panel of the thematic approach, **Sándor Richter**, senior economist at the Vienna Institute for International Economic Studies (WIIW) analysed the macroeconomic conditionality attached to cohesion policy transfers. According to the new MFF, all structural funds' money will be placed into the so-called "Common Strategic Framework" (CSF). Resources from the CSF will be fully available for only those member states which, on the basis of 11 scoreboard indicators plus 36 auxiliary indicators, display sound economic policies. Those member states which do not, can be placed under the macroeconomic imbalance procedure, and, if the situation remains unchanged for a predefined period of time, an excessive imbalance procedure can also be initiated against them. Ultimately, part or all of the payments from the CSF may be suspended. In a worst case scenario, where a member state is simultaneously under excessive deficit and excessive imbalance procedure, sanctions can reach up to 100% of the CSF funding or 1.5% of GDP. In addition, euro area members may, in case of violating the Stability and Growth Pact, be obliged to place a deposit ranging from 0.2 to 0.5% of their GDP. The negative impact of all these austerity measures will have a direct impact on the national budgets, and an indirect one on the national economy due to postponed investments. Now the big question is what will be the effect of all this in the member countries struggling with slow recovery.

The conference was concluded by **Miklós Somai** reminding the audience that a country's net budgetary balance can certainly not serve as a clear guidance when evaluating whether this particular country is, in financial terms, a net beneficiary of the integration or not. Free trade, investments made in the other member states, free movement of labour, and more generally, the advantages gained from the single European market and the common policies can largely compensate for possible losses associated with the EU budget, negative net balance and other quantifiable costs.

Prepared in Budapest, on 9 December 2013  
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