PISM | POLSKI INSTYTUT SPRAW MIĘDZYNARODOWYCH
THE POLISH INSTITUTE OF INTERNATIONAL AFFAIRS

BULLETIN

No. 11 (464), 6 February 2013 © PISM

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The February Budget Summit: The EU's Unfinished Business

Patryk Toporowski

At the upcoming European Council meeting, 7–8 February, negotiations on the Multiannual Financial Framework 2014–2020 may finally be wound down. For Poland, the overall outcome will be satisfactory in financial terms and may compensate for the EU's failure to reform spending through measures Poland can take at the national level. Yet, this lost opportunity for reform has broader political implications—it will further undermine the MFF as a programming tool. With such issues as a special fiscal facility for the eurozone the subject of future debates, Poland should work against fragmentation of the EU financing system.

The President of the European Council, Herman Van Rompuy, confirmed in mid-January 2013 that the EU's 7–8 February summit would be devoted to the finalisation of talks on the EU's Multiannual Financial Framework 2014–2020 (MFF). He also clearly stated that no new proposal would be presented, thereby ruling out a fifth draft compromise document (following the Commission's initial proposal) on how to divide the common funds. Despite some last-minute amendments, he seems to be staying firm and relying on the threat of provisional-budget rules coming into force to secure an agreement.

Unfinished Business. The IMF's recent admission that it had fundamentally underestimated the negative effects of belt-tightening during the crisis, and thus the impact of EU budget cuts on the bloc's struggling economies, might complicate the February discussion and disrupt Van Rompuy's plans by reopening questions about the best use of the budget. But technical economic arguments will play little part in the summit. In their bilateral talks with the president of the European Council, the heads of state and government have instead been concentrating on the factors needed to claim political victory at home. Moreover, during the summit negotiations themselves, political leaders will have only limited contact with advisors, something that creates a congenial atmosphere but limits their knowledge of the economic stakes. Agreement on a budget is more important than agreement on a technically sound budget. The desire to avoid the uncertainty of provisional budget rules is strong, as is the will to send a signal to voters that Europe is capable of action.

Since political expediency rather than sound economics is now the most important issue in the negotiation process, it is clear that some serious technical problems will be deferred. This is most notable for Common Agricultural Policy. The advertised "greening" of direct payments was dropped in January, and efforts to transform European farms into competitive enterprises, compliant with WTO rules, remain stunted. It is a similar picture for the revenue side of the common budget. The mooted introduction of a genuine system of own resources through an EU-wide Financial Transactions Tax (FTT) proved unacceptable for some of the Member States. Currently, with the acceptance of the ECOFIN Council (and in the face of British resistance), the FTT is the subject of enhanced cooperation between Germany, France, Italy, Spain, Austria, Portugal, Belgium, Estonia, Greece, Slovakia and Slovenia, and may generate approximately €37 billion per year. It is probable that some of these funds will be dedicated to development goals, such as France's declaration that it intends to allocate 10% of its income to the poorest regions in the world, a spending line covered by the MFF.

It is not just a failure to reform, however, that is challenging the MFF process. Major political issues have emerged that were not covered by the MFF format. The renewal of cooperation between Germany and France in the context of

completing the EMU, for instance, will have an important impact on the entire financing system through the emergence of a eurozone fiscal capacity. A relevant proposal discussed in December 2012 foresaw a rather small facility, designed for unemployment relief. However, the real discussion will start only after the closure of the MFF negotiations, meaning that the final shape and size could shift significantly. Similarly, the hardening of the British position on its EU membership also opens questions regarding the continued validity of the MFF format. The renegotiation of the conditions of the UK's membership in the EU would likely fall during the next MFF period, and additionally even before an EU budget review planned for 2016, which means that possible changes to the MFF would then have to take place.

Conclusions and Recommendations. At this stage of the negotiations it is difficult to change the MFF's design, especially given speculation that France has already made a deal with Germany on this issue. The principal change in any February deal would likely be a further decrease in funding. An additional lump sum decrease of €25 billion could be expected, resulting in total spending of €948 billion. Last-minute alterations may also negatively touch on cohesion policy, which in the November 2012 proposal was set at €320 billion. The budget for the still unreformed CAP, meanwhile, is not expected to fall below the level named in the last proposal—€372 billion—meaning the additional cuts would fall under headings little discussed among leaders, such as "Smart Growth," including the Connecting Europe Facility (down to €139 billion), "Security and Citizenship" (€17 billion), and "Global Europe" (€61 billion). For Poland, however, total revenue is expected to be €95 billion, with about €63 billion in net inflows. Bearing in mind the overall negative attitude of several Member States towards the size of the MFF given austerity-driven policies at national levels, this result is rather satisfactory for Poland.

But of course the amount of revenue is not the only issue. The more important question is how the negotiated funding will affect structural changes in Poland. In this, the proposed EU budget still aims too little at innovation, and the layer that administers EU funding discourages national and regional authorities from promoting competitiveness and innovation, preferring that funding go for infrastructure and public investment. The EU's failure to reform can, however, be at least partly offset at the national level. The Czech Republic has, for instance, successfully used Cohesion-related funds to make the economy "smarter," and now this country has significantly better innovation-related indices than other countries in the CEE. Poland might repeat this success by focusing more on small and medium-sized enterprises. This means encouraging the involvement of national and local authorities in creating and executing development plans, as well as engaging in thorough and timely auditing. Polish authorities should also encourage agents to apply for EU financing on innovative projects and provide knowledge on how to apply for the funds and help with finding project partners.

In a broader perspective, however, the picture is bleaker. Once again the chance to tailor a modern budget has been lost and a lack of political capital has hobbled necessary reforms. This has further undermined the MFF format whilst highlighting its inability to anticipate certain major developments, such as the British membership renegotiations, banking union and EMU completion. This is a sign of the change in the system of financing EU activities and of the increased variety of formats for deciding on the level and division of money. As a result, the size and importance of the MFF will decrease over time, i.e., not only through eurozone fiscal capacity but also via other indirect sources such as the European Stability Mechanism (ESM), financing through the European Investment Bank (EIB), European Central Bank (ECB), EU Emissions Trading Scheme, and others. Poland, which may perhaps become a net payer in the longer term, should still strive to maintain the significance of the MFF. The fragmentation of the budgetary setup into different decision-making processes dealing with particular financing sources is a sign of the emergence of exclusive groupings and exceptional arrangements within the EU—a trend which Poland should resist. Otherwise Poland would be deprived from the possibility of influencing the increasing part of the system of financing of the EU activities. For instance, even if it becomes a member of the eurozone it would take time to take several decisive seats in the ECB or ESM, linked with financial flows. Also within the MFF the changes are rather evolutionary than revolutionary, which is safe not only for Poland but also for the other Member States.