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The EU Budget's Mid-term Review

With Its Promising Reform Proposals, the Commission Lays the Groundwork for the Next, Post-2020 Budget

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The EU's Multiannual Financial Framework (MFF) lays down the amounts available for the EU budget over seven-year periods – currently about one billion euros for 2014–2020 – and at the same time it sets the EU's political priorities. The midterm review or rather revision offers a rare opportunity of reworking the established sums and adapting the MFF to new topical challenges. The Commission evidently wants to use this chance: on 14 September 2016, it presented an extensive package of proposals for reforming the MFF. This opens up the possibility of improving an unsatisfactory situation, in which the EU is unable to react to a changing environment or new crises with a policy that has a sound financial foundation, or re-orientate its budget. The revision also lays the groundwork for the negotiations on the new, post-2020 financial framework, which will begin in 2018.

The EU primarily sees its budget as an investment budget for pursuing medium-term political goals and for creating seven years of planning security and predictability for its multiannual programmes. Short-term shifts and even more so reprioritisations require unanimity and are therefore very difficult to achieve.

However, the European Parliament (EP) had insisted during the negotiations for the current MFF in 2011/12 that the Commission had to check and review the MFF's established priorities and financial provisions mid-term. According to Article 2 of the MFF regulations, the Commission is obliged to implement the task this year of reviewing the way the MFF operates and to present reform recommendations. Additionally, the Commission committed itself to revising the MFF regulations as part of this mid-term review and to checking the MFF's financial basis and duration. In other words, the Commission sought changes and adaptations for the second half of the MFF's period that far exceed a simple mid-term strength/weaknesses balance sheet. Such a far-reaching revision offers an opportunity of amending the MFF and the spending priorities set in the EU budget – with the proviso that EU funds already allocated to the member states cannot be cut. The majority of the MFF resources will thus remain unchanged, for the EU budget is characterised by the fact that 80 percent of its financial

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resources are allocated to expenditure headings at the very start of the MFF's term and firmly committed to the member states. Fixing expenditures in this way has the advantage that member states can predict with a very high degree of precision how much money to expect from Brussels and for which areas of spending. On the other hand, the migrant crisis in particular has shown up the disadvantages of the EU's lack of flexibility in budget policy, which results from fixing the MFF's spending priorities and total amount for seven-year periods. The massive need for funding short-term measures could not be adequately met using the EU budget; a fast reaction to acute challenges and crises was almost impossible.

The European Commission's proposal

The Commission submitted its proposals for the mid-term MFF revision at the same time and in coordination with the State of the Union speech of its President Jean-Claude Juncker, on 14 September 2016. It suggested budgeting additional funds, especially for the areas of growth and employment, investment, and migration and external-border protection (see overview, p. 3). Overall, the spending proposed by the Commission for 2017–2020, the three remining years of the current MFF, amounts to 12.8 bn euros: 6.3 bn euros of additional funds and 6.5 bn euros either re-used or in de-committed appropriations. According to the Commission, the maximum spending ceilings agreed when the MFF regulations were adopted in December 2013 will not be exceeded. Apparently, however, it intends to release existing special funds – such as the solidarity or globalisation funds – from the straitjacket of the MFF ceilings, to manage them above the MFF ceilings and thus create more leeway for payments within these limits. In all, the package of proposals contains a communication, an extensive explanation, four legislative proposalsand a series of further proposals for adapting existing regulations, such as those on the early prolongations and replenishing of the European Fund for Strategic Investments (EFSI) and the Youth Employment Initiative. Some of these proposals will require unanimous decision-making, such as the amendment of the MFF regulation or the recommended new special funds, while the adjustments and restocking of the existing instruments will require approval by qualified majority voting, such as the increase of the European Fund for Strategic Investments (EFSI). The Commission intends to reach an agreement on parts of the MFF-review package by the end of this year, such as the top-ups requested in an amending letter to the draft general budget 2017.

In contrast to the European Parliament's demands, the European Commission does not intend to mobilise additional sums by explicitly raising the ceilings of the MFF expenditure headings. Instead, it wants to use unallocated finances that would otherwise flow back into the member states' budgets. It is nonetheless unclear which policies are supposed to yield up these additional financial resources, and where in the EU budget the Commission discovered them. It is likely that there are unallocated – and therefore potentially re-usable – resources in those MFF headings for which the Commission does not intend to mobilise any additional monies at the mid-term review. This is the case with the Common Agricultural Policy (CAP) in heading 2 and administrative costs in heading 5. Sources in the Commission say that personnel costs will be almost 2 bn euros lower by 2020 than was forecast when the MFF was adopted. However, in the upcoming negotiations the Commission will first have to show that there are indeed some 4.7 bn euros of unallocated funds left in the CAP heading.

The EU budget's flexibility instruments, which are expected to be used in case of crises and new tasks, have all been used up halfway through the MFF's term, leaving virtually no room for manoeuvre for unforeseen measures. The EU thus has no margins left at its disposal for reacting to

Overview
Financial volume of mid-term MFF revision for financial years 2018–2020

Commission mid-term review proposals for additional funding		Million euros (in current prices)
Heading 1A		
"Competitiveness for growth and employment"		**1,400**
– Horizon 2020	400	
– "Connecting Europe" facility (transport)	400	
– Erasmus+	200	
– COSME (SME funding)	200	
– Prolongation of EFSI (investments)	150	
– WIFI4EU (digital agenda)	50	
Heading 1B		
"Cohesion for growth and employment"		**1,000**
Youth Employment Initiative		
Heading 3		
"Union citizenship, freedom, security and justice"		**2,549**
Heading 4		
"Global Europe"		**1,385**
– Partnership framework process	750	
– European Fund for Sustainable Development	250	
– Macro-financial assistance	270	
– External lending mandate	115	
Draft annual budget 2017 – additional spending		**1,822**
Technical adjustment of cohesion-policy envelopes		**4,642**
Total of mid-term review package		**12,798**

From: European Commission; COM(2016) 603 final,
http://ec.europa.eu/budget/mff/figures/index_de.cfm#documents.

changes in its political environment. Knowing this, the Commission puts special emphasis in its proposals on new and better equipped flexibility instruments. It wants to replenish the exhausted funds and expand them, and even establish additional ones.

The Commission proposes to double the financing of the existing flexibility instruments and the Emergency Aid Reserve, and to remove the overall ceiling on the leeway for re-allocating monies. The Commission also proposes to create a new crisis reserve, to be financed by unallocated resources from all MFF headings. The Commission expects an amount of 3 to 4 bn euros per year. Member states experiencing an acute and grave crisis would be given specific above-average support from these reserves.

The gap between commitment appropriations and outstanding payments is increasing all the time: in late 2014, it reached 24.7 bn euros. To limit this discrepancy, the Commission proposes to establish a specific flexibility instrument for payment appropriations. The instrument would make it possible to transfer funds that will foreseeably not be allocated in 2017 to the 2018–2020 annual budgets, when needs are predicted to be noticeably higher, even if this shift meant exceeding the MFF's upper limits.

Negotiating the review proposals

In the coming months, member states will debate the Commission's proposal in the Council and then with the European Parliament. The Council has already created the necessary working structures, such as a Friend of the Presidency group. The Slovak presidency of the Council has already submitted a report on the state of play of the work in this working group and aims to finalise the negotiations on the amendment of the MFF regulation by the end of its presidency. The final negotiations between Council and Parliament are scheduled to finish in mid-2017 at the latest, so that the proposed modifications can come into effect on 1 January 2018.

Even before the Commission presented its proposals, a few member states had drawn up informal position papers and sent them to the Commission so as to influence its internal voting and decision-making process. The net contributors (Germany, France, Austria, Denmark and the Netherlands) as well as the Visegrad Group sent their own position papers to Brussels, and the European Parliament also expressed its ideas in an early resolution. Given the positions adopted in the various papers and documents, negotiations look set to be difficult.

In the EP's initial report, adopted on 28 June 2016, MEPs called for a significant raise of all the expenditure ceilings laid down in the MFF. They pointed out that additional funds were especially necessary for coping with the consequences of the migration and refugee crisis, and for prolonging the terms of the European youth initiative and the EFSI, the so-called Juncker funds. Fundamentally, the EP does not expect the Commission to provide only a mid-term review of the MFF's weaknesses and flaws, but to carry out a more comprehensive revision, and especially to produce an amended MFF for the second half endowed with a noticeably higher expenditure volume – in other words, a de facto new MFF.

However, the member states had made it clear in their position papers that this was precisely what they did *not* want and that they intended to hold on instead to the MFF's basic principles and existing financial framework. They stated that if it became necessary to adjust the MFF for new political challenges, it should be possible to do so within its fixed ceilings by re-allocating funds and through more efficient budget management. However, the member states will face difficulties and will have to struggle to identify the areas in which such savings and redeployments are supposed to be made.

Any adjustment or modification of the MFF regulations requires the European Parliament's approval and a unanimous Council decision. If this consent is not possible, the MFF remains unchanged and continues to be valid as adopted. Because of the unanimity requirement, member states are in a powerful negotiating position vis-à-vis the Parliament. However, MEPs can be expected once again to combine two budget-negotiation dossiers into one overall package. In its proposal, the Commission has already established a link with the adoption of the 2017 annual budget. In turn, this connection with the negotiations on next year's budget strengthens the EP's position in the MFF adjustment negotiations, since the member states have a strong interest in seeing next year's budget passed on time.

The Commission has found a balanced compromise with its proposal to provide about 13 bn additional euros to meet the challenges raised by the current crises, but without changing the existing MFF ceilings. It is unquestionably necessary to plan additional sums for tackling the refugee crisis and the social consequences of the economic crisis, and to increase the EU budget's flexibility, which will mean expanding the margins. However, net contributors will surely – and emphatically – raise the question in the Council as to where this surprisingly large amount of new money will come from, especially since they remain to be convinced that unused funds should stay in the EU budget and spent on new tasks. Normally, monies in the EU budget that are not needed for programmed projects are not allocated and returned to the member states, that means they are set off against the future payments member states have to make to Brussels, in accordance with their financing obligation under the own-resources system.

In this context, controversial discussions should be expected between Council and EP on adjusting the MFF and re-using unallocated funds, or at least refraining from returning them. Moreover, member states are likely to clash in the Council on how to set priorities for the additional sums. Which task is paramount and needs additional monies most: substantially raising spending on the joint refugee and migration policy or on fighting youth unemployment? Can unused funds for promoting the CAP be used for other tasks? Or should European farmers, on the contrary, receive stronger support out of the EU budget, given their falling incomes and the loss of export markets brought about by the EU's sanctions against Russia?

The Commission, too, has secured itself a strong political mandate for these foreseeable conflicts. The contents of the mid-term MFF revision, Commission President Jean-Claude Juncker's speech on the state of the Union, and the Bratislava roadmap are linked and reveal a certain amount of parallel prioritisation. This suggests that there will be enough political pressure to make the necessary financial resources for concrete projects available with the MFF adjustment. These projects will surely include reinforcing external-border and coastal protection, managing third-party agreements on preventing migration, and prolonging the EFSI and the EU's programmes for tackling youth unemployment.

Perspectives for the post-2020 financial framework

In the context of this comprehensive revision of the MFF, a number of issues and topics are already taking shapefor the upcoming adjustment of the next MFF post-2020. They will be relevant for the formal negotiations on a new MFF, slated to begin in 2018. The European Commission will have to submit its proposal for the post-2020 MFF by the end of 2017. To prepare its MFF package, the Commission usually schedules a consultation phase, during which it incorporates demands and proposals from the EU institutions and member states as well as European civil society. This period of reflection on the post-2020 MFF began with the mid-term revision. The Commission, EP, and several member states have already presented their thoughts on the topics to be given priority in the discussions. Seven key points are becoming apparent:

(1) *Modernising the EU budget:* the priorities for the EU's spending policy will, as usual, be at the very top of the agenda for the next MFF negotiations. For the net contributors, this means above all aligning EU expenditure more closely with the principle of European added value and clearly emphasising the need for greater efficiency and more effectiveness. Their main goal is to use EU funds to reach the EU's common growth and employment targets and strengthen competitiveness. That would mean linking the EU budget more closely with the economic coordination processes that are running in the framework of the European Semester. The Commission is attempting to do justice to this approach by making budget management more performance-orientated. By contrast with the net contributors, it sees a European added value above all in the funding programmes that it manages itself. The Visegrad states and other net beneficiaries, however, specifically reject this emphasis on centrally administered EU programmes; in their opinion, the European added value is primarily to be found in the EU structural funds and the CAP.

At any rate, very different contents and targets are associated with the expression of "European added value". Over the past decade, the search for a common definition has been unsuccessful despite repeated attempts. The next MFF negotiating round will nonetheless make a renewed effort to find a common reorientation of spending policies.

(2) *MFF flexibility:* In the past year, the EU has shown itself incapable of providing quick and comprehensive financial assistance out of the EU budget to the member states worst hit by the migrant crisis. As a result, there were increasing calls for making the EU budget more flexible. The MFF negotiations will have to find a new relationship between the necessary ability to react quickly to new political challenges and the medium-term predictability of the EU budget. This can be achieved through additional flexibility instruments – meaning new funds for unforeseen tasks – as currently proposed by the Commission, or through simplified possibilities for redesignating and shifting resources between expenditure headings (which would, however, reduce predictability for the member states). In any case, the MFF negotiations must come up with a solution to this problem that is capable of achieving consensus.

(3) *The duration of the next MFF:* The EP continues to demand that the MFF's term be adjusted to match the Commission and Parliament political mandate periods. Its objective is to politicise the procedure and thus strengthen the MFF's democratic legitimacy. In 2011, the Commission backed by the EP had already suggested a 5+5-year term for the MFF; however, the member states did not follow up on the proposal.

Every modification of the MFF term raises fundamental problems for reconciling it with the EU's multiannual funding programmes. It is hard to predict the political implications of a changed term. The EP, at least, is hoping to politically strengthen its negotiating position.

To date, in its proposal the Commission has always staked out the frame and structure of the next MFF and laid the foundations for the negotiations in the Council and with the EP. Since MFF negotiations take about two years, adjusting the MFF term means that it would always be the "old" Commission's job to provide a budget for the "new" Commission. It is uncertain whether the successor Commission would feel bound by its predecessor's political prioritisations. The result would presumably be to weaken the political importance and binding nature of the Commission's draft MFF, which would be tantamount to weakening the Commission's right of proposal and role.

(4) *A budget for the eurozone:* Many reflections on how to develop and lastingly stabilise the economic and currency union are increasingly linked with the MFF – especially the idea of creating a separate eurozone budget. Both the Commission and EP want to use the next MFF negotiations to debate such a separate budget. The proposal for a specific euro-zone budget with its own institutions (eurozone finance minister, eurozone parliament) could threaten the unity of the EU budget. Alongside the question of *whether* this is feasible, two further questions about *how* it could be done need to be answered. Would a eurozone budget be part of the EU MFF and therefore subject to EP scrutiny? And would the MFF ceilings apply to the eurozone budget as well?

(5) *Reforming the financing system or introducing an EU tax:* Before the end of 2016, a group of experts led by Mario Monti will submit its final report on reforming the EU own-resources system. The report is expected to discuss and make recommendations on the controversial idea of introducing an EU tax. The European Parliament's and the Council's positions are entrenched: the EP has been asking for years for such an autonomous source of resources for the EU budget, while a majority of member states forcefully reject the idea in the Council. What is certain, however, is that the topic will be on the agenda for the next MFF negotiating round.

(6) *Reforming decision-making processes*: MFF negotiations have been following the same pattern for over 25 years, and the results are usually sub-optimal and unsatisfactory. The European Commission, MEPs and a number of member states are therefore challenging the process for adopting the MFF.

It is under discussion whether the Council might be able to pass the MFF regulations by qualified majority decision rather than unanimously, which would limit the opportunity for member states to veto any compromise and thus complicate decision-making. The European Parliament also wants to prune back the dominant role of the European Council of Heads of State and Government, which has so far been using its own compromise to predetermine the position of the Council of Ministers in the following legislative process. The possibility of linking the annual budgets and the MFF more closely, as an additional means of reforming the procedure, is also being discussed.

However, the decisive question is whether the negotiating process can shake off the member states' focus on their respective national net balance, which currently dominates everything.

(7) *Brexit and its implications for the EU budget*: The current financial framework is unlikely to be affected by the United Kingdom leaving the EU. However, negotiations on the next MFF will need to take into account the loss of this substantial net contributor. In 2014, the UK was the third highest net contributor after Germany and France, with a negative net balance of 4.9 bn euros. The financial gap created by its exit can be closed either by reducing spending funds or raising the payments of the remaining net contributors. A combination of both options is likely. The MFF negotiations must therefore find a relationship between reducing expenditures and increasing payments that is capable of achieving consensus.

It is foreseeable that Germany's negative net balance will continue to increase. Moreover, the net contributors' negotiating positions, and especially the way Germany conducted the MFF-negotiations, have been significantly weakened. The UK's hard and often rigorous negotiating manner offered Germany an opportunity of presenting its own negotiating targets as a compromise solution. This opportunity for negotiation tactics has now been lost.

Inversely, the fact that the British budget rebate no longer applies makes it possible to improve the coherence of the EU budget system, and eliminate every rebate and other special rules. It is possible that the Brexit negotiations will not be concluded by 2019. In that case, the EU could conceivably resort to drawing up two alternative MFFs, one for the EU 28 and one for the EU 27.

Conclusion

Now that the Commission has presented its proposals, the mid-term MFF revision will become a central issue of European politics in the coming months. The pragmatic proposals offer a realistic path towards the necessary adjustment of the MFF. At any rate, the European Parliament and the Council welcomed the package, seeing it as a good basis and starting point for the legislative negotiations between the two institutions.

The Commission has established the right political priorities, which had also been presented by the member states in the Bratislava roadmap, and equipped them with adequate financial resources. Concentrating on replenishing the MFF's flexibility instruments and margins also received widespread support among those involved in the negotiations. In this, the Commission has resisted the EP, which wanted to propose a marked raise of the MFF ceilings. It thus also refrains from placing further strains on the national budgets. However, it remains unclear where in the EU budget the total sum of about 13 bn euros of available monies, as calculated by the Commission, might be found.

With its package of proposals on the mid-term MFF revision, the Commission has resumed its classic role of mediator between Council and Parliament. It is to be hoped that it will be also able to play this role in the negotiations for the new MFF, starting in 2018.

It is now up to these two institutions, the Council and the European Parliament, to ensure a swift implementation of the Commission's proposals. All those involved in the negotiations between the two legislative bodies – and with the usual conflict between net contributors and net beneficiaries in the circle of member states – should therefore seek a quick compromise, rather than push to have their maximum demands met.

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