"Dimitrie Cantemir" Christian University
Knowledge Horizons - Economics
Volume 6, No. 2, pp. 91–99
P-ISSN: 2069-0932, E-ISSN: 2066-1061
© 2014 Pro Universitaria
www.orizonturi.ucdc.ro

THE COHESION VERSUS BETTER SPENDING DEBATE DURING THE NEGOTIATION OF THE EU MULTIANNUAL FINANCIAL FRAMEWORK 2014 – 2020

Alexandru HUZA

Faculty of International Economic Relations, 'Dimitrie Cantemir' Christian University, Bucharest, E-mail: alexandru.huza@mae.ro

Abstract *The paper reviews the negotiations on the EU multi-annual financial framework (MFF) for 2014 - 2020 which took place between 2011 and 2013 and involved all EU member states and institutions. Focus is put on the debate regarding the funding of the Cohesion Policy, which emerged as the most contentious issue throughout the negotiation process. By following the reasoning lines of the coalitions built around this controversial issue and how the diverging interests were accommodated to allow the advancement of negotiations, it concludes on the significance of the achieved compromise for the EU growth and convergence related goals, as well as with respect to the inter-institutional balance and the relations between member states within the European Union.*

Key words:
EU Budget, Multi-annual Financial Framework (MFF), Cohesion Policy, European Institutions, intra-EU negotiations
JEL Codes:
F15, F36, F55

1. Introduction

The multi-annual financial framework (MFF) for 2014 – 2020 is the EU budgetary planning tool over the next 7 years, laying down the maximum annual amounts ('ceilings') which the EU may spend in each major political field ('headings'), with implicit impact on financial contributions and allocations for each member state.

The MFF package comprises an expenditure side, structured on major headings (1.Smart and Inclusive Growth, which includes structural and cohesion funds, but also spending related to EU research and education programmes; 2.Sustainable Growth: Natural Resources – covering expenditure under the Common Agriculture Policy; 3.Security and citizenship; 4.Global Europe; 5.Administration) and a revenues side (traditional own resources such as agricultural and custom duties and a part of the VAT collected by member states, as well as, up to about three quarters of total revenues, national contributions by member states based on the gross national income). The MFF is also part of a more comprehensive package which also comprises a set of sector-specific legislations defining the conditions of eligibility and the criteria for the allotment of funds for each EU spending programme.

The aim is to provide a framework for financial programming and budgetary discipline by ensuring that EU spending is predictable and stays within the agreed limits, as the annual budget are to be adopted within this framework and usually remain below the MFF expenditure ceil. The multi-annual financial programming also allows the EU to carry out common policies over a period that is long enough to make them effective [1].

In relation to national budgets, the distinctive role of the EU budgetary planning consists in financing investments where important economies of scale can be reached, steering national policies, but also co-generating investments from private and public sectors. While deemed small and insufficient to address the crisis in Europe [2], the EU budget is the principal financial instrument for joint action by member states to face common challenges.

In this context, the negotiations of the MFF, which took place between 2011 and 2013, combined three complex elements: the debate on the long-term budgetary exercise, the prioritization of shared policy goals and the balancing of a wide range of political interests of the main actors with influence over the decision making process (namely member states seeking to protect areas of the budget from which they do well, EU institutions seeking to maintain and expand their competencies, European and national lobbying groups trying to gain access to financing opportunities).

The main phases of the negotiation process, further presented, were: the launch of the debate with the submission of the legislative proposal for the MFF by the Commission in June 2011; the intergovernmental negotiation, dominated by coalition building and polarised debates over the size of the budget in general and funding of the Cohesion Policy in particular, which was completed by the political agreement reached at the European Council in February 2013; and the inter-institutional negotiation between the EU Council and the European Parliament, resulting in the adoption of the MFF package in November 2013.

2. The starting point of the negotiation – presentation of the European Commission's proposal

The negotiation process started in June 2011 with the presentation by the European Commission of the first draft of the legislative proposal for the MFF, shortly followed by proposals relating to the legal basis for European spending programmes in almost all policy areas. Subsequently, an amended version of the MFF was published in July 2012.

Basically, the Commission proposed a draft EU budget for the financial programming period 2014-2020 amounting to 1,033 billion euro (around 1.05% of the EU GNI), which represented an increase of 5% compared to the EU budget for 2007-2013.

As significant savings were provided by the already agreed reform of the Common Agriculture Policy (downsized to 36% from 41% of the total expenditure during 2007–2013), funds were proposed to be reallocated towards other headings. Thus, funds for research and innovation were to increase with 46% compared to the previous programming period), while other increases were also provided for security and citizenship, external action and administration related spending.

A moderate increase was also provided for the second main chapter – the Cohesion Policy (up to 36,7% from 35% of the total budget in 2007-2013). However, this amount included 50 billion euro reserved for a future infrastructure fund (Connected Europe Facility) that would work completely differently from programs traditionally co-financed by the structural funds.

Also related to the funding of the Cohesion Policy, the Commission proposed to reduce the capping from 4 to 2.5 per cent of the Gross National Income for cohesion allocations and added, as a new element, the Transition Regions with a per capita GDP of between 75 and 90 per cent of the EU average, benefiting from a "safety net" of structural funds money amounting to at least two thirds of their allocations during the MFF 2007–13. At the same time, unitary algorithms applied to regions by the Commission resulted in noticeable re-directing of funds between recipient countries, which actually were mostly correcting differences in per capita allocations of the previous programming exercise. Thus countries like Romania, Bulgaria, Slovakia and Poland were to benefit from additional funds, while other beneficiaries such as Spain, Italy, Portugal, Greece and Hungary were about to suffer significant cuts (though from a higher initial level)[3].

In general, the proposals presented no radical changes in the structure of the EU budget, but made an attempt to improve the quality of strategic planning and policy implementation, aligning expenditures with the Europe 2020 objectives.

Still, two main novelties were put forward by the Commission: the macro-economic conditionality and the proposed reform on the revenues side.

The first was the macro-economic conditionality in relation with the cohesion policy funding, meaning that even budgeted-for structural funds could be suspended for member states conducting inappropriate economic policies, including the failure to adopt measures deemed necessary to correct the excessive deficit. Inspired from the conditionality enshrined in IMF stand-by programmes, the idea had been promoted by the net contributors to the EU budget (especially Germany) and enthusiastically picked by the Commission, as it was meant to strengthen its ability to enforce EU economic governance.

The case for macro-economic conditionality consisted, according to the Commission and its other supporters, in the fact that cohesion could not be separated from the wider context of economic policies and failing to implement macroeconomic policy guidelines was linked to inefficient use of structural funds; thus, it needed to be sanctioned with withholding EU funds payments and/or commitments until the deviation was corrected.

But, while conditionality is justified for the IMF loans aimed precisely at macro-stabilization, transforming the absorption of EU funds into de facto stand-by arrangements is problematic with respect to their objective of achieving growth and convergence, considering the prospect that already severe fiscal problems might be worsened by withholding funds that could be used for improvement or that the ultimate recipients (mainly regions and municipalities) would be punished for failures at government level. Thus, it cannot be expected from structural funds to simultaneously correct macroeconomic imbalances and address social and cohesion related problems in an effective manner. Also, the type of macroeconomic coordination is to be questioned, as rules that govern macroeconomic coordination are hardly politically neutral, being designed to favour a pro-austerity economic policy, and therefore any suspension of EU funds based on macroeconomic conditionality would be a political decision, strengthening the position of actors favouring such policies, namely Germany and other like-minded states and the European Commission, in relation to the recipients of cohesion funds.

The second controversial issue proposed by the Commission referred to the attempt to increase the EU budgetary autonomy through direct financing from new sources (a financial transactions tax and a reformed

VAT resource to replace the existing national VAT contributions), as well as its transparency by replacing the current mechanism of rebate/corrections with one based on lump sum reductions to net contributors' payments.

The rebate/corrections mechanism originated in the British rebate obtained in 1984 as compensation for the UK's disproportionate net contribution to the Common Agriculture Policy and to account for the UK's relative wealth compared to the other member states. The rebate was to be covered by the other member states, but Germany, the Netherlands, Sweden and Austria negotiated corrections of 25% on the share they had pay towards the rebate, leaving France and Italy (as main beneficiaries of the Common Agriculture Policy) to pay a higher share. However, as CAP spending started to shrink as a proportion of the EU budget and the UK became relatively wealthier within the EU, questions were raised, mainly from the European Parliament, on the utility of maintaining such a complex and less transparent mechanism, which led to the reform proposal by the Commission.

3. The funding of the Cohesion Policy - central issue of the inter-governmental dissension

As in previous MFF negotiations, the tension between austerity demands and national necessities arose against the background of a renewed phase of the economic and financial crisis economic crisis in Europe, which imposed member states to pursue effort for harsher budgetary rigor and financial discipline [4].

The bargaining power of the member states and the unanimity rule, according to which each state has a veto and could thus block the final agreement, determined the outcome of the intergovernmental negotiation.

As the debate on a reformed own resources system has gradually waned due to inconsistent support from member states and was postponed at an early stage of the negotiation process, the most contentious issue became the funding of the Cohesion Policy, namely the EU structural and cohesion funds conceived as the main instrument of growth to allow the poorer members to catch up with the relatively well-off. Together, the funds represented the second largest expenditure item (after the Common Agriculture Policy) between 2007 and 2013 and were supposed to pass first during the next programming period, according to the Commission's proposal. While aimed at helping poorer regions in the EU catch up with richer ones, spending under Cohesion Policy also covers other side objectives, such as social cohesion, competitiveness along the lines of the Europe 2020 Strategy and the protection of the environment.

Net contributors to the EU budget, naming themselves "Friends of Better Spending", took a strong and inflexible position aimed at consistently reducing the overall MFF level. Their pledges were to carve from 100 (Germany) up to 200 billion euro (UK) of the a bit more than 1 trillion proposed by the Commission, through cuts that could not leave out the Common Agricultural Policy and/or the Cohesion Policy, which together were constituting the bulk of spending, given that the other items had little scope to either increase or reduce.

But as France, one of the main members of the constituency, insisted to protect CAP spending from further cuts and concluded a deal with Germany in this respect at an early stage of the negotiation, the main pressure was put on the cohesion policy, especially since many of the net contributors were questioning the extent to which cohesion funds were useful for the economic growth in the EU.

Indeed, the effectiveness of structural funds, as presented in various impact studies based on econometric models, reveal an ambiguous picture in the sense that some studies report a positive impact, while others a non-significant or even a negative one [5]. A case was made that EU funds could actually slow convergence if the associated wealth effect increases demand for leisure and decreases labour supply, as the combination of higher consumption and crowding out of investment results in relative price adjustments, inducing a temporary bout of Dutch disease[6]. Also, effectiveness of structural funds is conditioned by the quality of governance in general and of public administration institutions in particular.

Moreover, although the structural funds are designed to help poorer areas catch up with richer ones, all regions, even the richest ones, are eligible for at least some funding. As a result, a substantial part of the funds still goes to the EU wealthiest member states, defined as those member states with a GDP per capita at 90% or above the EU average; that could be a potential source of savings [7].

Based on this kind of assumptions, "Friends of Better Spending" claimed that their main goal was be to optimise spending for the cohesion policy through downward pressure, as with fewer funds available, the recipients' preoccupation for their better spending must amplify. Thus, they embedded within the concept of better spending (to be applied only to the Cohesion Policy) pledges for capping allocations, but also for insertion of macro-conditionality (proposal supported by the Commission, as shown above) and the diminution of the pre and co-financing rates.

However, their real objective was to reduce the overall size of the budget, in order to reduce pressure on the revenues side reform, which could threaten the rebate/corrections mechanism. In fact, states benefiting from this system (UK, Germany, Austria, Netherlands and Sweden) made clear that they would use their veto right to block any attempt to dismantle the current arrangement, while Denmark requested for a correction of its own contribution. Not incidentally, precisely these states have adopted the harshest position with regard to the spending for the Cohesion Policy, while France and Italy have taken a more conciliatory stance towards the net recipients' demands.

A reason for the net contributors' reluctance towards increasing contributions to the EU budget was linked to the emergence of new requirements for participation in mechanisms designed to safeguard financial stability within the euro area established outside the EU budget framework, such as the European Stability Mechanism (formed by subscription from members of the Euro zone amounting to 700 billion euro) or the yet to be established Single Resolution Fund for rescuing troubled banks. But these requirements only apply to members of the Euro area and funds are to be provided by their banking sectors, apart from the public budget contributions to the EU budget.

A secondary common goal of the Friends of Better Spending group, also meant to improve their net financial balance, consisted in redirecting of a part of the potential savings resulted from cuts in cohesion spending towards increased EU research and development funding, based on arguments such as the superior added value compared to other EU spending areas. That was not surprising, since the richest EU countries host the leading research institutes and the most innovative companies, best positioned for accessing grants from the excellence – based EU R&D Framework Programme.

In response, net beneficiary states (Romania, Bulgaria, Czech Republic, Greece, Cyprus, Malta, Spain, Portugal, Estonia, Latvia, Lithuania, Slovenia, Slovakia, Poland and Hungary) reactivated the Friends of Cohesion Policy Group (which had been formed in 2004 by the new member states plus Portugal, Greece and Spain in order to secure the role of Cohesion Policy in the negotiation of the MFF 2007-2013). During the negotiations for the new financial framework, Cyprus left the group after taking over the EU Presidency in the second half of 2012 in order to assume the position of honest broker, while Croatia, which participated in the negotiations as an observer, joined in.

The Friends of Cohesion Policy organized throughout 2012 three high-level meetings in Bucharest, Bratislava and Brussels, releasing joint statements in favour of maintaining at least the current levels of spending for Cohesion Policy in order to effectively act against current disparities among the various regions of the EU. The group also wanted flexibility, empowering member states to use the assistance as they know their own needs the best, measures designed to increase their absorption capacity (co-financing and pre-financing rates at least at the levels proposed by the Commission, VAT eligibility for all projects, extension of the execution period) and were concerned by what macroeconomic conditionality could mean.

There were, however, a number of potential areas of discord within the group arising from the economic outlook and their attitudes towards EU integration, influencing their behaviour in the MFF negotiations. For instance, some were enjoying special relations with other EU Member States, whether bilateral, as with Germany or UK, or to groups of states, such as Euro zone members, susceptible to undermine their loyalties to the Friends of Cohesion Policy Group and induce them hope of benefiting from special arrangements. Then, there were differences in their economic structure, with some boasting large agriculture sectors or sectors with particular structural needs, or in their openness towards further EU integration which, coupled with a strong or weak economic position, were influencing their readiness to accept whether the EU gains greater competences.

Countries which joined the EU in 2004 and 2007 were also asking for a fairer distribution of CAP payments (under the present system the wealthier EU15 members receive substantially more per hectare), request not well received by older EU members in the group.

Besides, while the least developed member countries were asking to be granted priority in the allocation of funds and were reluctant towards specific measures in favour of countries having suffered from a significant GDP decrease, the relatively wealthier members of the group were against concentrating cohesion funds on the poorest states and were pushing for maximum accessibility of this policy to all regions and countries. A compromise formula was negotiated within the Friends of Cohesion Policy Group just prior to the group's summit in Bucharest in order to keep Spain, Portugal and Czech Republic within, conceding that while funding must be used to assist the least-developed regions, a look can be taken at a mechanism to phase out assistance as growth occurs and gaps close.

All these above mentioned differences gave them very specific interests in the structure of the budget, beyond their common interest in its overall size, significantly affecting the positions of individual members of the Friends of Cohesion Policy Group during the negotiations. These diverging interests could (and eventually would) be used by the better organized net payers, united under the one goal of top cutting the EU budget, to thwart attempts at a common position, by picking off individual members of the Friends of Cohesion group through proposals favouring some net recipients at the expense of the others.

In this respect, it was alleged that net recipients were facing a "prisoner's dilemma": by cooperating and maintaining their allegiance towards the group they could achieve the most beneficial deal to all but, if any of them would break rank and pursue a narrow set of interests in order to achieve an even better net national position, everyone would lose [8].

Among the Friends of Cohesion, stood the very vocal position of Poland – informal leader of the group – which stated its firm intention to veto any cut or unfair allotment of the cohesion funds. Poland also conducted considerable diplomatic efforts to alleviate diverging interests within the group and to initiate contacts, on behalf of the group, with the main net contributors, France and Germany. In contrast, the Czech Republic distanced itself from the other Friends of Cohesion by pushing for two demands — a lower overall budget and strong cohesion policy – thus acting as member of both the Friends of Cohesion and Friends of Better Spending groups, including through signing conflicting non-papers created by both groups of countries, which signalled its intention to follow a two-track strategy until its status of future net beneficiary is clarified.

On the whole, the Friends of Cohesion countries maintained their unity on the main point of contention with the net contributors - the size of the cohesion spending. Their main negotiating tactic consisted in arguing that cohesion could contribute to economic growth not only in the new members' states but also in the net payers' economies, as a consistent part of the structural and cohesion funds would get diverted to rich countries in form of contracts, boosting jobs and demand for raw materials, technologies and services. Also, they pointed to the beneficial impact of structural funds on their own development which, by creating new markets for companies from the all other member states, would translate to higher long-term growth across the EU.

On the other hand, Friends of Cohesion failed to take into consideration the full implications of their own arguments, in that in an institutional context unfavourable for the allocation of cohesion funds towards the productive sectors (*tradables*) of the economy and amid the loss of competitiveness through currency appreciation and/or higher inflation when inflows exceed what is needed to mobilize unused domestic resources (not the case of the current economic slowdown, but very much so for the EU periphery prior to the crisis), net payers' economies might gain most from cohesion spending through single market mechanisms, leaving net recipients less competitive and more dependent of fiscal transfers from the richer nations in the EU. In this respect, the "better spending" feature could have been a useful instrument for net beneficiaries as long as it wasn't understood merely as an excuse for cuts, but mainly as an effort to use the structural funds to narrow the competitiveness gap with knowledge based economies by upgrading labour skills, boosting technological endowment and getting better infrastructure. That even more so considering that inadequate financial allocations (both in terms of size and of effectiveness), but also improper spending of funds in favour of unjustified personal or group earnings, risk jeopardizing the net recipients' chances of reaching targets under Europe 2020 Strategy, already lower than those established at Community level, which would lead to widening disparities across the Union [9].

In their endeavour to reduce the competitiveness gap, an improved participation in the EU Research, Innovation and Technological Development Framework Programme (Horizon 2020), whose expansion was favoured by the net contributors, could have spawned opportunities for the less developed members to connect to the global innovation networks, but it is difficult, due to insufficient capital, for their research units to compete with research leaders from western Europe, thus risking to end up as net contributors to the EU budget for research and development, which would mainly finance projects in wealthier member states [10]. Therefore, the Friends of Cohesion group opposed the transfer of funds towards European R&D programmes, as long as the very competitive financing rules proposed by the Commission stipulated concentration on excellence instead of projects aimed at helping them build the capacities needed in order to successfully access grants.

In fact, the diametrically opposed views of the Friends of Cohesion and Friends of Better Spending groups with regards to the financing of the Cohesion Policy and competitiveness enhancing programmes show that at the origin of the dividing line between net payers and net recipients stand cleavages within the EU arising from co-existence of two different business models. Namely, while Western and Northern European economies are based on products and services with high added value, incorporating cutting edge technology, the Southern and Eastern EU periphery is dominated by the production of standardized goods, with less added value, these states being less able to cope with global competition, with their lack of competitiveness being aggravated by brain drain, which makes it most difficult for them to change their development paradigm. More than the division between newer and older member states or between members and non-members of the Euro zone, the co-existence of the two economic models, each with its own specific needs in terms of financing priorities, but also of macroeconomic, regulatory or foreign trade related policies, poses the greatest risk for the devolution of the EU into a two-speed Europe.

4. The advancement of the negotiation process and its outcome

During 2012, the Danish and later Cypriot Presidencies of the EU Council attempted to narrow down member states' positions by holding bilateral meetings and presenting compromise options on conflicting issues. As versions of the negotiating box were being circulated, Commission's proposed ceilings were being adjusted downwards, at the request of the net contributors, with cuts from all headings. This approach was criticized by the Friends of Cohesion group, whose members expressed support for the Commission's version. However, they failed to offer enough support to the proposed reform on the revenues side, which could have created financial space for the desired level of spending.

At last, member states expressed their willingness to reach an agreement at a special European Council held in November 2012 and solely devoted to the MFF 2014-2020. The task of mediating cleavages between members was taken over by the President of the European Council, who presented a compromise proposal providing 970 billion euro in global expenses over the envisaged period, about 65 billion euro less than the Commission's proposal. Cuts were distributed among headings (about 20 billion euro from the Cohesion Policy, 17.5 billion euro from the Common Agricultural Policy, and about 10 billion euro from each of Competitiveness, Connecting Europe Facility and External Action).

In order to make the proposal seem satisfactory to as many as possible members of the Friends of Cohesion group, cuts in the Cohesion Policy were operated through means precisely designed to disintegrate the net recipients' bloc. Thus, at Netherlands proposal, a "reverse safety net" mechanism was introduced, which led to a double-capping of cohesion funds at both 2.35% of GNI and 110% of allocations during the 2007 – 2013. Only two countries – Romania and Slovakia, which were supposed to benefit from a considerable increase of funds compared with the previous programming period – were harmed by this mechanism, which left some funds available for side payments to compensate countries (such as Spain, Italy and Hungary) whose allocations were supposed to decrease from the 2007 – 2013 level. However, in compensation, Romania and Slovakia were promised solutions to reduce the risk of automatic de-commitment arising from their poor absorption of funds from the 2007-2013 national envelopes (thus not affecting the overall 2014–2020 MFF). Furthermore, countries hardest hit by the crisis, such as Greece and Portugal, were allowed a slight increase of the absorption limit up to 2.59% of GNI.

The country loosing most from this arrangement was Romania, whose bargaining position was already uncomfortable, as it was enjoying the highest increase of the national allocation proposed by the European Commission compared with the 2007 – 2013 period (up to 40%), which made it a target both for the net payers, in order to downsize the overall cohesion ceiling, and for the net recipients whose national allocations were to be diminished and were looking for sources of compensation, despite the fact that these diverging displacements of national allocations compared to the previous period were meant to merely alleviate the extreme disparities of per capita allocations between member states (as during 2007–2013 Romania's allocation per capita was less than half than those provided to Greece, Hungary, Czech Republic or the Baltic states). Moreover, due to the extremely low rate of absorption and irregularities in spending the funds, Romania was vulnerable to other attempts of capping cohesion spending, such as a previous (eventually dropped) proposal of the President of the European Council of correlating the allocations with the absorption performance in 2009-2011. On the other hand, even with the double-capping of cohesion funds, Romania was still receiving the highest increase of the national allocation compared to the previous programming period – from 33.6 to 39.4 billion euro - as to the 10% increase in structural and cohesion funds were to be added further gains from the gradual convergence of direct payments under the Common Agricultural Policy, being thus most interested in the conclusion of the negotiations. Therefore, while criticizing the reverse safety net mechanism as discriminatory and contrary to the convergence and cohesion objectives of the EU, Romania moved in, along with Slovakia, towards securing a firm assurance from the European Council regarding the amending of existing regulations to allow the extension of the execution period of the on-going projects under risk of automatic de-commitment, which offered it a last chance to benefit from as much as possible of the funds available for 2007–2013.

In the end, although the compromise proposed by the President of the European Council was tacitly accepted by the two informal leaders of the opposing coalitions (respectively Germany and Poland), a general political agreement could not be reached, as UK (under strict mandate from the British Parliament to defend acquired rights such as the British rebate and to insist on additional cuts), Sweden, the Netherlands and Denmark pushed for further lowering of the MFF size, while other member states, including France and Italy, threatened to use their veto if main headings were to be further reduced. It was agreed, however, that further efforts would be pursued to identify potential savings of up to 30 billion euro from chapters less affected so far (such as administrative expenses), provided that Cohesion Policy and Common Agriculture Policy were protected from additional cuts, in parallel with accommodating, as far as possible, the top one or two priorities (red lines) of each Member State in order to make possible a consensus at the beginning of 2013.

Indeed, in February 2013, the European Council agreed on the Multiannual Financial Framework covering the period between 2014 and 2020. In the version validated by the European Council, expenses of the Union composed of 28 member-states were limited at 960 billion euro in budgetary commitments, which corresponds to a mere value of 1% of EU's Gross National Income, down with approx. 3,4% in real terms from 995 billion euro for 2007-2013. Thus, for the first time in history, the Union's multiannual budget has decreased in comparison with the previous programming period [11].

As for the MFF structure, spending for Cohesion policy was diminished with about 30 billion euro compared with the previous 7 years, in addition to 70 billion euro cuts from the financing of the Common Agricultural Policy. As net payers proposed, but not to the amount they (and the European Commission) desired, part of the savings (about 35 billion) were re-directed towards competitiveness enhancing programmes. Macro-economic conditionality was also decided upon as part of the final compromise.

On the other hand, the Friends of Cohesion group succeeded through coordinated pledges in securing a set of favourable conditions for the absorption of cohesion funds, such as extension from 2 to 3 years of the maximum execution period, 85% co-financing rates, reimbursement of VAT related expenses for all projects, facilities for countries under macro-stabilization programmes and additional funds for regions with highest rate of youth unemployment.

The agreement also left the revenue side almost unchanged compared to the current situation because of the impossibility to reach unanimous agreement on any major changes. UK, Germany, Austria, Netherlands, Sweden and (for the first time) Denmark received the right for corrections to avoid that they pay too much in relation to their relative prosperity.

Thus, the European Council of February 2013 set the political mandate for the EU Council in the negotiation of the MFF regulation with the European Parliament.

The Lisbon Treaty had enhanced the role of the European Parliament in the negotiations over the EU long-term budget by giving it the right of approval or rejection of the MFF regulation, but not the right of amending. Nevertheless, the European Parliament regarded the MFF negotiation as a good opportunity to re-assert its political ambitions, by demanding that member states should incorporate its opinion expressed in various resolutions and position papers issued before the conclusion of the inter-governmental agreement. Thus, it had called for an increase of the new MFF of at least 5% (up to 1.1% of the EU GNI) over the 2007 – 2013 programming period, exceeding the Commission's proposal, as well as for a substantial reform of the revenues side for the budget to be part-funded directly by EU taxes and the rebates that UK and other countries were enjoying to be gradually removed. As the European Parliament's calls were in line with the position of the Friends of Cohesion Policy group, Germany and the other net contributors opposed to their taking into consideration throughout the negotiations within the European Council, arguing (not without reason) that it was unlikely for a qualified majority within the EP to take the responsibility of rejecting the MFF regulation.

Still, one month after the agreement achieved by the European Council, the European Parliament adopted by large majority its own negotiating mandate, which called for the rejection of the MFF, unless certain essential conditions were met, namely maximum overall flexibility and transparency, revision of the MFF in 2016 and an ambitious agreement on own resources. [12] In fact, the European Parliament's mandate was based on the acknowledgement that it could not question the negotiated amounts, so instead had to focus on improving the way the MFF is executed, by attempting to mitigate the lower ceilings through higher flexibility.

The request of higher flexibility came from recognizing the need to mitigate problems arisen from the rather inflexible character of the 2007-2013 financial framework, which in the first years generated surpluses that were returned to the national budgets. But, in the second half, as more projects were implemented and more beneficiaries were asking for refunds, the EU budget execution resulted in growing payment deficits that needed to be covered through additional contributions, which main payers, already under fiscal pressure induced by the economic crisis, were inclined to postpone. Therefore, the European Parliament insisted that deficits for 2012 and 2013 should be financed prior to the adoption of the new MFF, so that the new budget cycle should start without any funding gaps. Furthermore, to avoid recurrence of similar troubles, the European Parliament demanded a that higher MFF flexibility should be provided for the next period, through the possibility of front-loading and back-loading certain budget lines and the use of global margins carryover from one year to another (which also gives the EP stronger competence in adjusting the MMF execution by amendments to the annual budgets).

Related to the flexibility issue was also the request that the next legislature EU institutions should be able to undertake the revision of the MFF in 2016 in order to evaluate the new flexibility measures and the effectiveness of frontloading of growth-generating programmes (such as the initiative of fighting youth unemployment), as well as to supply the EU budget with new funding, if necessary. That was a reasonable demand, given that a seven year budget needs to take account of changing economic circumstances, but the European Parliament went even further by asking that the revision should be legally binding, enshrined in the MFF Regulation and decided by qualified majority in the Council. If adopted, it would have meant the opening of a path towards qualified majority voting with respect to MFF (traditionally adopted by unanimity), which could have led, through the possibility of isolating UK, to increased chances of reforming the revenues side, a long standing goal of the European Parliament.

Throughout the inter-institutional negotiation between the EU Council (the body representing the interests of the member states) and the European Parliament, the countries within the Friends of Cohesion policy group were facing a political dilemma: on the one hand, the EP demands were favourable to the net recipients of structural funds, as a higher degree of flexibility would facilitate the absorption of the allocated amounts through re-allocation of unused funds between years and operational programmes, while the advancement of the own resources reform and the gradual removal of corrections would create opportunities for additional funds in the future; on the other, they were bound by the political mandate already agreed by the European Council and, furthermore, feared that a disunited approach of the Council would have prolonged the negotiations with the EP and delayed the adoption of the MFF regulation, jeopardizing the launch of the new operational programmes at the beginning of 2014. Thus, they adopted a positive, though cautious, approach towards proposals such as the increasing of flexibility and transparency and discussing a roadmap on rethinking the way the EU budget is financed, aimed at facilitating the consent of the European Parliament, while agreeing with the net contributors on the need to ensure the consistency of the final regulations with the European Council Conclusions agreed in February 2013.

In the end, the EU Council accepted to some extent part of the EP requests, such as funding of the current payment deficits, a higher degree of flexibility and the 2016 revision (but without the qualified majority voting), as well as the establishment of a high-level group on own resources reform, although not binding commitments regarding the timing and substance of such reform were made. The inter-institutional agreement led to the adoption of the MFF legislative package in November 2013, opening the path to implementation starting in January 2014.

5. Conclusions

As negotiations were held against the challenging context of a renewed phase of the economic and financial crisis across Europe, completion of the process reflected the recognition by the involved actors, beyond their specific sets of interests, of the need to avoid the foreseeable consequences for the cohesion and credibility of the EU of a failure to make decisions on such major issue.

The tense debate between net contributors and net recipients over the size of the budget in general and financing of the Cohesion Policy in particular was settled in favour of the more united net contributors, as proven by the decrease, for the first time in history, of the Union's multiannual budget in comparison with the previous programming period, the structural change of expenses in favour of priority areas for the wealthier states to the detriment of the Common Agricultural and Cohesion policies and the maintaining of the complex and un-transparent correction mechanism.

Thus, in relation to the complex needs of the member states and to the requirements related to the implementation of the Europe 2020 Strategy, which would have required both more funds and improved quality of spending, but also in comparison with the more fair and growth oriented initial Commission's proposal, the outcome of the negotiations can be assessed as suboptimal, signalling the conversion of the EU from a prosperity union, traditionally oriented towards growth, employment, competitiveness and convergence, into an austerity union, whose members focus on national net balances rather than on common purposes.

However, the rather selfish and inflexible approach from the part of the net contributor states has to be understood as deriving from the concerns raised by their own citizens, amid domestic fiscal consolidation efforts, with regards to the prospect of expanding payments to the benefit of other member nations. In the absence of a common sense of identity and solidarity among European citizens, the prospect of balancing the more advanced monetary integration within the Economic and Monetary Union with further steps towards fiscal integration, including through a consolidated EU budget, needs to be reconsidered.

In terms of inter-institutional balance, the negotiation process emphasized the role of the European Council, which has been the main determinant of the resulted compromise. Although its institutional role, as defined by the EU Treaty, is to provide the Union with the necessary impetus for further development through negotiation skills and informal cordial relations between leaders, the European Council has traditionally acted as a platform used by the more or less euro-sceptical European leaders to enforce the inter-governmental control over the integration process, including by preventing other European institutions to expand their competences. Thus, as also observed during the MFF negotiations, the European Council tends to generate suboptimal compromise solutions based on looking for the least common denominator, which may be worrisome considering the complex challenges that need to be addressed at this level related to on-going intra-EU negotiations on key issues, such as the establishment of the Banking Union, the adoption of long-term climate and energy targets or the coordination of EU reaction to international political crises.

As for the Friends of Cohesion policy group members, although their joint efforts to cope with the constant pressure from the main contributors to reduce the EU budget and the funding of the cohesion policy have achieved only a limited success (the agreed MFF still being a reasonable compromise in terms of cohesion share in the overall budget and conditions for accessing the funds), it remains as a net gain the maintaining of coherence and unity throughout the entire negotiation process. Building upon the achieved level of mutual trust, it would be in the joint interest of the net beneficiary to meaningfully expand the areas of cooperation beyond the budgetary negotiations, by addressing other issues equally important for their common goals in the context of the on-going negotiations related, for example, to the Single Market (to cope with transfer pricing and rent extraction practices by hosted transnational companies), Banking Union (to reinforce the say of the host countries in the regulation of transnational financial groups) or the 2030 Package on energy and climate change (to ensure a fair burden sharing and compensatory measures with regard to the EU greenhouse gas emissions target, given the higher pressure placed on convergence countries). By doing so, the net beneficiary member states would also enhance their coordination during the yearly budget negotiations, which are still important since annual budget expenditures are systematically lower than the MFF ceilings.

References

[1] European Commission, The Multiannual Financial Framework explained*, available at* http://ec.europa.eu/budget *updated: 05/02/2014*

[2] Kölling, M. (2012) „The Multiannual Financial Framework 2014 – 20 – Best European value for less money?" Perspectives on Federalism, vol. 4, issue 3, 2012

[3] European Commission, (2012) Amended proposal for a COUNCIL REGULATION laying down the multiannual financial framework for the years 2014-2020, COM (2012) 388 final

[4] Kölling, M. and Serrano Leal, C. (2013) „Towards an Agreement on Growth and Job Creation? The Multiannual Financial Framework 2014 - 20 on the Agenda of the European Council of 7-8 February 2013", *Area: Europe ARI 4/2013*

[5] Zaman, Gh. and Georgescu, G., (2009) „Structural Fund Absorption: A New Challenge for Romania?" *Romanian Journal of Economic Forecasting – 1/2009*

[6] Allard, C., Choueiri, N., Schadler, S. and Van Elkan, R. (2008) „Macroeconomic Effects of EU Transfers in New Member States" *IMF Working Paper/08/223*

[7] Swidlicki, P., Kullmann, A. and Persson M. (2012), *SEIZING THE MOMENT: Aligning the EU budget with Europe's economic needs,* London: Open Europe

[8] Kalan, D., Tokarski, P. and Toporowski, P. (2012) „Visegrad's Winding Road to the EU Multiannual Financial Framework 2014–2020" *PISM Policy Paper No. 39/2012*

[9] Huza, A, (2013) „Europe 2020 Strategy - 2 years after release", *Metalurgia International Vol. 18 Issue 4/2013*

[10] Huza, A, (2011), *The New Economy in the New Europe. Transition towards Knowledge Based Economy in the New EU Member States from Central and Eastern Europe*, Bucharest: Curtea Veche

[11] Conclusions of the European Council on the 2014-2020 MFF, 8 February 2013

[12] European Parliament, (2013) Resolution on the European Council Conclusions of 7-8 February 2013 concerning the Multiannual Financial Framework, 2012/2803(RSP).