

National "Red Lines" Undermine European Budgetary Reform



By **Dr. Phedon Nicolaides**¹, Professor – EIPA Maastricht

The discussions among Member States on the budget of the European Union for the period 2007-2013 have reached an impasse. Member states want to keep as much as possible their receipts from the budget, while at the same time reducing their contributions. Naturally, this is not a solution that can apply simultaneously to all of them.

The member state which is in the most awkward position is the UK. For domestic political reasons, the UK government refuses to make concessions on an outdated and indefensible instrument of the EU's budgetary arrangements, which is known as the UK "rebate".

The rebate was introduced in 1984 as compensation to the UK for not having a large agricultural sector and for trading extensively with non-EU countries. At that time, close to 80% of the EU's expenditure went to farming and about half of its revenue came from tariffs on imports of non-EU products. The UK, with its traditional links with the Commonwealth and North America, paid a disproportionately large amount into the EU budget and received a disproportionately small amount from Brussels.

Regardless of the fact that budgetary surpluses and deficits are partial and misleading indicators of the benefits and costs of EU membership, all Member States have drawn their "red lines" in the current negotiations on the Financial Framework for the period 2007 to 2013. The large net payers such as Germany, France, the Netherlands and Sweden and the UK demand a reduction in overall expenditure. Ironically, the UK also wants to maintain its rebate. Naturally, the net recipient countries do not want to lose their subsidies. Any way you see it, money to or from Brussels is important in domestic politics. Even the eurosceptic Polish farmers are reported to have softened their views after receiving subsidies from the EU's agricultural fund.

In the absence of any cohesive vision, the opposing claims will probably degenerate into coarse bargaining



with the same results as in previous budgetary negotiations. In the end, any agreement on the 2007-2013 Framework will be a mixture of compromises without much logic.

There will be no long-term solution, unless the EU deals with the problems on the expenditure side of the budget. This is because EU spending is a patchwork of policies some of which have become obsolete. By contrast, on the revenue side, the contributions of the Member States are largely based on a reasonable principle: the size of

- their economies and therefore their relative wealth.
- Successive GATT rounds have also meant that tariffs now generate a very small proportion of EU revenue so they hardly skew payments by member state.

- On the expenditure side, the UK Treasury published in March 2003 a paper that made a number of sensible proposals on how to rationalise EU spending. Eighty per cent of that spending goes to farming and structural projects mostly in poorer regions. The Treasury paper argued for concentration of structural expenditure in the most needy regions of the Union. It rightly asked, why recycle funds through Brussels.

- The Commission proposals which are presently being negotiated also advocate similar concentration. But they have two grave flaws that undermine the logic of concentration. They grandfather all currently eligible regions and they make funding available to poor regions in relatively rich countries.

- Regions such as Western Ireland have per capita incomes that far exceed the threshold of eligibility for regional funds, which stands at 75% of EU average income. Yet they will continue receiving EU financial support simply because they receive it today.

- Other regions with per capita income below the threshold of 75% are located in relatively rich countries such as Belgium, Sweden or the UK all three of which have per capita at about 117% of EU average.

The EU should support those policies that make it more cohesive, more competitive and give it a more effective voice in the world.

The principle of cohesion, which is enshrined in the EU Treaty, suggests that structural funding should be allocated to Member States according to their need which translates into their ability to provide financial resources for the growth of their poor regions. The EU should support those Member States which do not have that ability. Solidarity would then mean support for poor regions in poor countries – not just poor regions irrespective of whether they are located in poor or rich countries. Rich Member States with poor regions can mobilise domestic resources for the development of their underdeveloped regions. As the Treasury paper asked, why recycle funds through Brussels?

On agriculture the UK views are well known. It prefers elimination or drastic reduction of subsidies to farmers. But this has implications for its rebate that need to be drawn out. When agricultural funding was mostly in the form of output subsidies – i.e. before the reforms introduced in 1992 – it did make sense to centralise support through the EU budget. Otherwise there would have been large distortions of competition.

Now, however, that funding is largely de-coupled from production and will be even more so in the future, there is hardly any justification for centralised funding. Member states can indeed give income supplements to their farmers without distorting competition. This means that most agricultural spending can and should be re-nationalised. It would reduce significantly overall EU expenditure and at the same time remove the need for the UK rebate.

The problem is that France opposes vehemently any

The time has come to end both the UK rebate and recycled funding for farmers and regions of rich Member States.

reduction in agricultural spending. In fact, in October 2002, France and Germany pre-empted any meaningful EU reform by undertaking a commitment to maintain agricultural subsidies at their present level until 2013. At the same time, France wants the UK rebate to be phased out. This in itself is an untenable position.

The EU has a last chance to rationalise its budget before the next enlargement will make it virtually impossible. Both Bulgaria and Romania have relatively very large agricultural sectors and it is obvious where they will draw their red lines.

Despite the apparent intransigence of national positions, it is rather clear what

kind of reform makes sense for the EU in the longer term. The EU should support those policies that make it more cohesive, more competitive and give it a more effective voice in the world: i.e. structural actions, research and development, external action and development aid.

The time has come to end both the UK rebate and recycled funding for farmers and regions of rich Member States. Perhaps it may be possible for France to accept lower support of agriculture if the UK would give up its rebate. If that could happen it would rationalise the budget of the Union and would make the most significant contribution to streamlining EU policies.

NOTES

¹ The views expressed here are purely personal. ::