WISO DISKURS

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László Andor

RESOURCES FOR A PROSPEROUS EUROPE

Redesigning the EU Budget in a Progressive Way

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FOREWORD

In May the European Commission presented its proposal for the new Multi-annual Financial Framework of the European Union (EU) for 2021 to 2027 and its financing. The Multi-annual Financial Framework is the key instrument and core element of the common European budget policy and reflects the EU's policy priorities. It lays down both the total budget and its allocation among the various policy areas for a seven-year period. The presentation of the European Commission's proposal also ushers in the negotiation phase. When this is concluded both a majority in the European Parliament and all member states in the European Council must give their assent to the final proposal so that the new Multi-annual Financial Framework can come into force.

The presentation of the proposal for the new Multi-annual Financial Framework and the attendant negotiations come at a time when the EU is facing a whole raft of major internal and foreign policy challenges. These include continuing regional disparities and increasing economic divergences, persistent high unemployment, increasing inequalities of income and wealth, an influx of refugees and strong migration pressure, threats and insecurity in the wake of terrorism, new military conflicts and geopolitical changes, globalisation alongside increasing protectionism, advancing digitalisation, climate change and resource scarcity, demographic change, the need to stabilise the euro-zone, and, last but not least, Brexit.

The European Commission is well aware of these challenges and, within the framework of its proposal, besides a slight increase in the total budget, has instituted a careful rebalancing of resource allocation, away from agricultural subsidies and cohesion policy towards more resources for, for example, foreign and security policy, research and innovation policy, migration and development policy, as well as stabilisation policy. The main emphasis here is the provision of public goods by the EU, which represents a significant European added value, while at the same time proposing increased financing of the EU budget through new own resources, but also greater use of funding instruments, more budgetary flexibility and closer linking of the disbursement of EU budgetary resources to new conditionalities.

It remains to be seen, however, whether the Commission's proposal will be sufficient to meet the current challenges and to what extent, ultimately, agreement will be reached. In the course of the negotiations, as so often, the member states' different expectations and interests will come into conflict, regarding both the overall size of the budget and the allocation of budget resources to the various policy areas and spending programmes. The fear is that the negotiations, as in the past, will be dominated more by the conflict between net-contributor and net-recipient countries than by the urgent need to focus on the pressing challenges and the European added value of the EU budget.

In this context the Friedrich-Ebert-Stiftung asked Professor Dr László Andor, former EU Commissioner for Employment, Social Affairs and Integration and currently – among other things – Associate Professor at Corvinus University in Budapest, to provide a progressive perspective on the European Commission's proposal for the new Multi-annual Financial Framework, as well as progressive proposals and starting points for its further development, based on expert discussions and specialist workshops.

The hope is that this study will give rise to further discussions around the new Multi-annual Financial Framework. The negotiations should focus not on the question of who pays how much into the EU budget and who gets how much out of it, but rather on the question of how the EU member states can, by means of joint European action, best tackle the current economic, social, environmental and political challenges and thus make a better job than it has so far of satisfying the expectations and needs of all EU citizens. EU membership offers all participating states a substantial added value and other benefits that are not reflected in national net balances. This can be realised and maximised by means of a future-oriented EU budget, thereby enhancing Europe's prosperity.

We hope you will find this paper both interesting and informative.

MARKUS SCHREYER
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PREFACE

This study was written to provide a progressive perspective on the budget of the European Union, including an exploration and critique of the new long-term EU budget proposal (or Multiannual Financial Framework, MFF) of the European Commission.

The paper offers a systematic overview of the MFF and the first reactions to the new MFF proposal in May–June 2018. It does not cover all details but tries to identify the critical discussion points and the directions of progressive change.

Another hope behind the study is that it will help to engender further comments, questions, ideas, reactions and clarification regarding the MFF and its various chapters. This should directly feed into the debates and negotiations restarting from September 2018 and expected to intensify ahead of the European Parliament elections in 2019.

In this study, the assessment of the new MFF proposal will be carried out with reference to:

- recent analysis by experts (especially those linked to progressive politics and think tanks);
- the history of the EU budget and various financial instruments;
- the personal experience of the author in EU policymaking and the supervision of the European Social Fund in particular.

The last point explains any thematic bias in this paper, but prospective readers have no reason to be put off.

The author is grateful to all those colleagues who attended FES and FEPS workshops focusing on this topic and contributed with comments to the production and finalisation of this paper in the spring and summer of 2018.

1

INTRODUCTION

The preparations for the new long-term EU budget (or Multiannual Financial Framework, MFF) in the second half of Jean-Claude Juncker's term of office at the European Commission coincided with broader deliberations about the future of the European Union.

Thanks to the coincidence of general elections in several member states (Germany and France, but also the Netherlands, Austria and Czechia, together with snap elections in Malta and the United Kingdom), 2017 became a year for reflection in the European Union. With almost no exception, the general question hanging over these parliamentary or presidential elections was whether an EU-sceptic, nationalistic breakthrough would take place or not. For many, only the extent of this shift was uncertain, and the 2018 Italian elections completed the cycle with the rise of an anti-Brussels coalition in one of the founding members of European integration.

A deeper soul-searching has also been stimulated by the impending departure of a major member state, the United Kingdom ("Brexit") and the external challenge to European integration represented by a disruptive new US President Donald Trump, together with the general instability of the EU neighbourhood with the never-ending Ukraine crisis and the aftermath of the 2015 refugee shock. Debates about the future of the EU have been supported and framed by the European Commission's White Paper (March 2017) and five "reflection papers".

Of the major political developments of recent years, it is Brexit that seems to have the strongest impact on the design of the newly proposed MFF, and it is a largely negative one. Fearful expectations about the aftermath of the UK referendum and similar reactions to the result have been pushing EU politics towards a defensive position, which has also affected the MFF proposal and the surrounding debates.

Progressive analysis and politics, however, also have to reflect a wider range of current and anticipated challenges faced by the European Union and draw appropriate conclusions. Even if the EU is bound to respond to Brexit, it also has to explore the causes of Brexit. Imbalances among and inequality within countries of the EU that have been sources of instability and disintegration in Europe call for progressive analysis, as well as EU solidarity in practice, supported by concrete fiscal competences and capacities.

In this paper we discuss some of the key issues of this debate, with the intention of making some practical proposals, together with more general political conclusions. We analyse the MFF from political as well as economic perspectives, followed by operational questions. This structure should help to put the budgetary debate in a new light.

The aim is not to design an ideal budget for an imaginary European (Progressive) Union. Rather it is to highlight the potential of the existing EU budget, which is a historical product, and to see what directions should be followed in case political support can be built for progressive improvement in the immediate debate or in the coming years.

2

THE POLITICS OF THE MFF: DEFINING SIZE AND STRUCTURE

Political analysis of the European Union usually explores the tensions between intergovernmental governance by the assembly of member state leaders and the national interests they represent, and a community orientation, which is represented by common goals, institutions and instruments of Europe as a whole. A political analysis of key questions of the EU budget should not differ. We need to look at the key national issues put forward in the budget debate and how common European solutions can develop and add economic and social value to the community of nations and citizens. The size of a budget is a pivotal political question, but whether it is big or small, its signalling function also has to be appreciated.

2.1 PUBLIC DEBATE AND LEGITIMACY: AMBITION AND DEADLINE

Debates about the long-term EU budget are cyclical. Every year there is a season for budgeting and auditing, and every time a new long-term budget is created (normally for a seven-year period) the costs and benefits of EU funding instruments are thoroughly discussed among member states, regions and other stakeholders.

In 2017–2018, the adoption of the new MFF proposal by the European Commission was preceded by a period of reflection on future alternatives[1] and some key questions of EU integration. Unfortunately, the lessons of these debates did not make a strong impact on the new Commission proposal for the seven-year EU budget (MFF). This is explained partly by the time frame in which the Commission finds itself during the second half of its mandate.

While there is understandable concern about the limited time available for approving the proposal before the 2019 European Parliament (EP) elections, we also need to discuss seriously whether the new budget would help to counter the trends of economic, social and political disintegration that have put increasing pressure on the structure of the EU. The size as well as the structure of the newly proposed MFF have to be scrutinised, together with the promise that a small budget line in the MFF can sufficiently address the question of euro-zone fiscal capacity.

The recent debates in EU institutions and political convulsions in various countries have also cultivated concerns about the democratic deficit in the EU. And from this point of view the pre-election adoption of the budget becomes an issue. If the MFF is a technical question, adoption before the next parliament should not raise concerns. On the other hand, the EP election campaigns can and surely will highlight issues with implications for the MFF. Various “Spitzenkandidaten“, assuming that the “top candidate“ mechanism continues, will have to make points and promises also in the area of the EU budget. This would make it awkward if the EU institutions close a major dossier at a time when citizens are expressing their views. The legitimacy of the new MFF might suffer if the new EP and Commission are seen as having been pre-empted regarding budgetary matters.

This point is particularly important from a progressive point of view. The Party of European Socialists (PES) started to outline budgetary priorities in the course of 2017, highlighting the importance of a robust Cohesion Policy, the need to support investment across the EU but especially in peripheral countries, the establishment of a euro-zone fiscal capacity and support for research, innovation and education. It is important to ensure that these issues do not get side-lined under pressure of time and that adequate attention as well as resources are devoted to progressive priorities.

Without holding back the whole process, an alternative scenario one might suggest is to complete the debates on most technical details but invite the participants of the EP elections to form a view on selected issues, such as the embeddedness and size of the euro-zone fiscal capacity, or the political conditionality attached to various instruments. On the basis of the outcome of the European Parliament elections, a rapid conclusion could be reached in 2019.

1 The White Paper of the Commission, adopted on the 60th anniversary of the Treaty of Rome, outlined five possible scenarios for the future development of the EU. The list included some that also allow for a withdrawal or retreat in territorial or functional terms.

2.2 PUBLIC DEBATE AND LEGITIMACY: THE TYRANNY OF THE STATUS QUO

The size and the structure of the EU budget should allow the EU to deliver on issues that the EU Treaties require it to address. This simple principle is established in Article 311 TFEU but its translation into practice is not that easy. First of all, the EU achieves results not only through funding; in fact it does not deliver primarily through funding, except in a few policy areas. The EU achieves results through legislation, policy coordination and budget, and funding often is the least preferred option. Second, besides those areas of action that are considered exclusively EU or national competences, the majority of policy areas can be found in between, namely policy areas of shared interest. For the budget this means that some could easily argue for much greater funding and others for a much lower level of common spending within the legal framework of the Union.

Thus theory alone never guides one to a solution that is consensually rational and desirable. Guidance, however, is always provided by the inherited situation or status quo. This very much applies to the Commission's new MFF proposal. In the 2017 reflection paper, five budgetary scenarios[2] were sketched out, to match the White Paper. The headings of the five scenarios were: 1. Carrying on, 2. Doing less together, 3. Some do more, 4. Radical redesign, and 5. Doing much more together. In the end, the MFF proposal 10 months later fell closest to "Carrying on", with a broadly stable volume and a general trend towards lower relative shares of cohesion and agriculture to finance new priorities, and a higher use of instruments and guarantees.

According to Iain Begg (2018) the Commission's proposals are not especially ambitious or radical, but go some way to meeting conflicting demands. Packaging aside, a realpolitik MFF has been put forward, especially as regards overall volume, although even this way the proposal touches on many sensitive areas and sets some new directions that will lead to heated debates.

The small size and the apparent fetish of 1 per cent fiscal centralisation is a source of constant frustration for many, especially those who expect a lot from the EU and believe that there is a value added to the money spent at EU level. The EU can be compared with the United States in terms of market size and global trade role, but it comes out a fiscal dwarf in a trans-Atlantic comparison. In such moments of embarrassment we have to remind ourselves that the United States was a political union from its birth, which is the coming into force of its Constitution in 1789. Economic integration has been a gradual process in post-war Europe, accompanied by delayed and incremental steps towards political unity, which is a pre-condition for fiscal integration under democratic standards. The European Parliament (EP) is not a real parliament in this respect (Leron 2018), because it does not have power to raise revenue from the citizens.

The EU is not a federal system, but is a form of non-federal integration linked by definition to a particular level of centralisation, such as 1 per cent. Interestingly, the famous MacDougall Report[3] in 1977 concluded that in a pre-federal stage, EU integration should soon develop a budget in the range of 2–2.5 per cent of total GDP (of the then nine members). If there is a next stage ("small public sector federal") at which monetary union is established, the Community budget should be in the range of 5–7 per cent, or 10 per cent if defence is also counted as a new Community competence.

The four decades since the MacDougall Report have seen immense developments in the functions and competences of the EU, including monetary union and an early stage of defence cooperation. Still, we are stuck at the level of 1 per cent, as if there was a glass ceiling preventing a further rise of fiscal concentration, and anything beyond should just happen in the court of policy coordination.

The EU that exists as a result of this is one with a big gap between ambition and capacity, bound to disappoint those who expect material intervention where a common interest and purpose is revealed. To give one example, when the Arab Spring broke out in early 2011, the EU designed a strategic response within six weeks. Regarding material support to democratising countries in North Africa, this went as far as offering EUR 10 billion from the European Investment Bank (EIB) and EUR 1 billion from the European Bank for Reconstraction and Development (EBRD), all in loans, which means that the actual budgetary capacity to take action vis-à-vis this "rendezvous with destiny" was miniscule.

Because of many shared competences, complementarity and supportive roles within the division of labour between the EU and its member states, it is often difficult to see the logic of having or not having EU resources available for a particular cause, and officials themselves may not be exempt from the confusion. As a long-serving member of the European Commission once noted: "first I was a commissioner with a budget but without a policy, and now I am a commissioner with a policy but without a budget".

The new MFF does not point towards breaking out of this state of ambivalence. However, an apparent standstill can be a product of conflicting pressures[4] towards increasing or decreasing overall volume, and for greater or smaller redistribution. In the preparation period for this particular MFF, the key question was to resist the downward pressure stemming from Brexit and its simplistic interpretation.

2 The five scenarios in the White Paper the reflection paper was supposed to connect with are: 1. Carrying on, 2. Nothing but the single market, 3. Those who want more do more, 4. Doing less more efficiently and 5. Doing much more together.

3 At the end of 1974 the Commission asked a seven-member group of independent economists, chaired by Sir Donald MacDougall, then economic adviser of the CBI (Confederation of British Industry), to examine the role of public finance at the Community level in the context of future economic integration. The Study Group held fourteen meetings from April 1975 to March 1977. Officials of several Directorates-General of the Commission also took part in these meetings (Economic and Financial Affairs, Regional Policy, Budget, Financial Institutions and Taxation). The Group also had the benefit of discussions with two expert consultants from the United States and Australia.

4 Because of the prevailing nationalist sentiment, Jean Pisani-Ferry (2018) describes the MFF debate as "a deeply depressing experience. All countries view it from the perspective of net balances – how much they receive, less how much they pay – without regard for the intrinsic value of spending. And, because wasting money at home is regarded as better than usefully spending it elsewhere, the composition of expenditures bears no relation to the EU's stated priorities."

One reasonable starting point for a discussion on the volume of the MFF would be the European Parliament resolution of March 2018 that "estimate[d] the required MFF expenditure ceilings at 1.3 per cent of the GNI of the EU-27" in an approach in which the current level of funding would be maintained for long-standing EU policies and new needs would be met with new resources.[5]

2.3 BREXIT AND THE SIZE OF THE EU BUDGET

The European Commission proposes a modest increase for the EU budget; altogether 1.11 per cent of the GNI of the 27 countries to be centralised. This modest increase, however, is qualified by the fact that the European Development Fund (EDF),[6] historically an extra-budgetary instrument, would be part of the MFF in the future. Producing an increased headline figure for the MFF ostensibly defies the discourse that emerged in the wake of Brexit which, from a budgetary point of view, would see a net contributing country withdraw from the EU.

The narrow victory of Leave over Remain in the UK referendum of 23 June 2016 ostensibly triggered a process of separation from the other 27 members of the European Union. Brexit, from a budgetary point of view, would remove a net contributing country from the EU. Simple arithmetic suggests that this would necessarily lead to a smaller EU budget and less funding for common EU policies. Expenditures also have to be cut and we urgently need to explore "how to do more with less". A general shake-up of the EU budget is justified (Haas 2017). Some commentators and politicians, typically in net contributing countries, quickly concluded that "a smaller EU needs a smaller budget".

However, a budget is not only a question of maths but also politics, and the Commission is right to reject the notion that the United Kingdom's exit by definition means less revenue and less funding for common EU policies. In 2013, the United Kingdom was one of four countries[7] that insisted on reducing the EU budget in net terms, after the Commission had proposed a modest increase. At a time of recession and investment drought, squeezing the EU budget was a bad message and unwise policy. Shortly afterwards, the Juncker Plan had to be devised to boost investment through common European financial instruments.

As the United Kingdom leaves, the group of countries that favour a smaller budget could become weaker, as long as all other countries maintain their earlier position. This, however, cannot be taken for granted. In 2018, several member states (such as Austria and Finland) signalled opposition to a budget increase that had not demanded a reduction in the previous round. In commentary on EU affairs, there is frequent reference to a "New Hansa", which means a number of smaller and medium-sized countries, mainly in the North, that oppose either a larger EU budget or risk-sharing in the euro-zone or both. EU-sceptic parties in these countries also use Brexit as the writing on the wall.

However, taking Brexit as a starting point for defining the size of the EU budget can be misleading. One should not forget that the United Kingdom's net contribution has not been as big as many believe. This is because of the extraordinary rebate won by Margaret Thatcher in 1984 at the Fontainebleau summit. In 2005, the United Kingdom accepted a reduction of the rebate of about one quarter of its value, in exchange for a commitment to a more general review of EU expenditures. If the United Kingdom leaves, this particular rebate would end but others[8] should do so as well. Rightly, the Commission is proposing to phase rebates out. Ending this obsolete practice would significantly lower (perhaps even halve) the budgetary loss in proportion to overall EU GDP, hence there is a need to look for additional revenues, where the Commission makes proposals for own resources, in other words, forms of revenue not taken from the budgets of member states.

Even if some countries remain modest, prudent or even sceptical about the EU's fiscal capacity, the overall size of the EU budget can and indeed has to be reconsidered, together with how exactly the money is raised. Eventually, Brexit may trigger a greater change on the revenue side as opposed to the expenditure side of the EU budget. Whether countries want more money to be raised or to uncouple specific functions from EU funding remains to be seen (Haas and Huguenot-Noël 2017).

A progressive approach would involve the abolition of rebates and the introduction of several new own resources, as also advocated by a majority in the European Parliament.[9]

2.4 BREXIT AND THE STRUCTURE OF THE EU BUDGET

Assuming that, in the absence of a "MacDougall momentum", the overall size of the MFF more or less remains the same, its internal dynamics become the real question in the short term. One way to approach this is to set new priorities as against the old ones. The obligatory reference to Belgian economist André Sapir describes the EU budget as an "historical relic", which is probably a judgement on its size but even more on its structure. Innovation is a virtue, and although it could also mean innovation within specific instruments, in today's discourse it means the reduction of existing large envelopes.

5 European Parliament resolution of 14 March 2018 on the next MFF: Preparing the Parliament's position on the MFF post-2020, P8_TA(2018)0075.

6 Created by the 1957 Treaty of Rome and launched in 1959, the European Development Fund (EDF) is the EU's main instrument for providing development aid to African, Caribbean and Pacific (ACP) countries and to overseas countries and territories (OCTs). Financed by direct contributions from EU member states according to a contribution key and covered by its own financial rules, it funds cooperation activities in economic development, social and human development, as well as regional cooperation and integration. The total financial resources of the 11th EDF amount to EUR€30.5 billion for the period 2014–2020.

7 Germany, the United Kingdom, Sweden and the Netherlands.

8 Other countries besides the United Kingdom have benefitted from rebates; in 1999 the Berlin European Council agreed to reduce the amount that Germany, the Netherlands, Austria and Sweden, the then net contributors, paid towards the UK rebate.

9 European Parliament resolution of 14 March 2018 on reform of the European Union's system of own resources, P8_TA(2018)0076.

The Common Agricultural Policy (CAP) and Cohesion Policy are today classified as "old policies" and together they represent more than 70 per cent of the EU budget. They are the dinosaurs of the MFF, and dinosaurs are supposed to die off, aren't they? Such policies are destined for extinction, if we are to make room for "new priorities", such as funding migration policies and actions required for stabilising the euro-zone. The Commission actually wants to push the combined share of CAP and Cohesion below 60 per cent, which appears to be a drastic move.

This approach in fact follows a historical pattern: in every cycle a modest reduction of the CAP has created room for new items. The share of the CAP in the total EU budget has been declining monotonously, decade after decade. In 1970, the CAP still represented over 90 per cent of total EU expenditure; in 1980, this share was already down closer to 70 per cent, while a decade later it was well below 60 per cent. By 2000, it still exceeded 40 per cent, but further decline was inevitable. This time the difference is that, together with the CAP, Cohesion Policy is also considered to be old and sentenced to reduction, despite the fact that in their contents and mode of operation these funds differ from one another considerably.

One should, however, doubt whether the job of the Commission is as simple as giving way to an irresistible decline of "old" policies, without properly assessing the changing needs they are supposed to satisfy. The need for food security, the stabilisation of rural incomes and to take care of our natural environment continue to uphold CAP politically, together with the case against competitive national schemes that could eventually be more costly than a common European one.

Behind the differentiation between old and new, one needs to notice the geographical implications of the proposed changes. Less spending on CAP and Cohesion, while more funding for the euro-zone and migration-related programmes would simply mean less systemic redistribution on the expenditure side of the budget. It would also generate a geographic shift by favouring the South and reducing allocations to the underdeveloped East. Amending the so-called Berlin method will have similar consequences. This is the main allocation formula in Cohesion Policy based on GDP per capita. If, for example, the youth unemployment rate is used to modify allocation, the South would get more, but without the direct obligation to implement a particular European policy in favour of young people.[10]

While ending all rebates would significantly lower (perhaps even halve) the budgetary loss in proportion to overall EU GDP, it is also true that how we spend has to be reviewed and improved in many fields. Stamping out waste, abuse and errors would be important anyhow, but it is even more pressing in the current circumstances. But what exactly is wasteful also depends on the political or ideological angle. Many, and especially supporters of "free trade", would consider the Common Agricultural Policy (CAP) pointless.[11]

Altogether, pitting old against new in the post-Brexit budget discourse appears to be a false trade-off. As Catiuscia Marini (2018) points out: "Even if a larger EU budget will be needed to keep the same share for cohesion policy, we cannot accept trade-offs between financing of new EU policies, such as defence, and cohesion policy-based investments in local and regional businesses, training courses for unemployed people or broadband connections for remote regions."

The structure and volume of the MFF should be driven mainly by an assessment of what the EU needs to do together.

2.5 POLITICAL ADVANCE: NEW PRIORITIES

While the current MFF discussions, due to the Brexit effect, usually start out from a defensive position, there is also a more positive narrative that provides the framework for a political counter-movement. This narrative is about the need and the capacity of the EU to finance "new priorities". The Commission has presented brave steps such as a significant increase of allocations in some strategic areas, but also with proposals for new own resources on the revenue side.

Following the Brexit referendum in the United Kingdom, defence and security was the first area to be identified by heads of states and governments in which the EU can and must do more, which is reflected in the new European Defence Fund (EDF) to help member states develop and acquire key strategic defence capabilities more quickly, jointly and in a more cost effective way. When introducing the EDF, President Juncker announced EUR 90 million still within the current MFF and an estimated EUR 500 million after 2020.

The post-Brexit redefinition of European defence cooperation coincides with renewed pressure from the United States for increased defence spending in Europe, and especially by Germany. Incidentally, Adam Tooze and Shahin Vallée (2018) also point out the dramatic asymmetry between the defence capacities of France and Germany, and call for a new bargain between them, ideally in an EU context. This is an inevitable debate and it needs to take place without Germany feeling condemned as a free-rider or as guilty for not being militaristic for over seven decades. US pressure on Europe to spend more in general has to be handled with care, however, because Europeans have too often had to clean up the consequences of US military decisions that they had no influence over. The United States may encourage Europeans to spend more on the military and the EU must promote some kind of internal rebalancing of security and defence-related contributions, but the latter must also insist on diplomacy and peaceful cooperation ("jaw-jaw") wherever it is a better alternative to military intervention.

Also among the winners of the new MFF is the Erasmus programme, whose total resources are set to double. Clearly, Erasmus has been a flagship EU programme in recent years. The 25th anniversary of its launch saw reports about its popularity and great cultural impact, as well as some demogra-

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10 Implementing a particular European policy in favour of young people (the Youth Guarantee) is a requirement for those who top up their ESIF allocations from the Youth Employment Initiative (YEI) in the current period. Disconnecting eligibility from a particular EU level policy framework would favour those who want EU money without EU policy, which is not the best way, especially with a budget that is so compressed.

11 From this point of view, Brexit may actually come to the rescue, because British public opinion has generally been on the CAP-sceptic side and it will be harder to claim that the CAP is wrong because Her Majesty the Queen is ultimately the greatest single beneficiary.

phic effects. The potential has been seen before: the Barroso II Commission proposed a 70 per cent increase and was given 40 per cent by the budgetary authority. With enhanced funding after 2020, Erasmus also promises to become more inclusive and accessible. Increasing the participation of students from poorer backgrounds (or those with other types of disadvantage, such as disability, health-related conditions or geographic remoteness) is an important promise.

Developing and harnessing the potential[12] of Erasmus is important but it should not lead to the mistaken thought that this would be primarily a policy for developing higher education. This is a mobility programme which, though unique and precious, adds very little to the attainment of the Europe 2020 targets on higher education. The development of infrastructure in education remains the responsibility of the ERDF and investment in vocational training and modernisation of the content of education remain in the remit of the ESF. In other words, those concerned with funding education should also focus on Cohesion Policy, and if that is allowed to erode just because some deem it to be an "old" policy that would also pose a risk to education.

While doubling Erasmus is a political choice, more resources for supporting migration-related policies and activities appear necessary. An Asylum, Migration and Integration Fund (AMIF) exists, but the Commission is proposing to more than double the size of this envelope (+225 per cent) from 2020. Given the crises, disputes and cleavages in recent years, this will be a small turf with big fights in the coming period, not so much because of the amount of money involved, but because of the shape and size of the EU level policy it is meant to support.

It would be a gross exaggeration to claim that the immigration debate in the EU is an artificial one, but it is surely inflated in the sense that the problems related to asylum and immigration have been instrumentalised in various domestic political disputes. While it is true that the pressure on Europe has been minor in comparison with the burden on Jordan or Lebanon, the 2015 refugee crisis was a real shock to European societies and all the different concerns in this context have to be addressed. At the same time, it has to be noted that the gap between perception and reality has widened since then, and in budgetary terms it is the reality and not the perception that needs to be addressed most of all.

It also needs to be appreciated that in this round of immigration debates the topic, as many times before, has served as a distraction from the failures of economic policies and social systems. Immigrants are the easiest scapegoats for unscrupulous politicians, and this has played out in full in recent years, whether it be intra-EU migrants or refugees from other continents. More precisely, inflating the refugee crisis on the political stage, including by connecting it to the experience of terrorism, has served right-wing politics in its effort to wind down the discourse on inequality. The latter has been promoted by public figures as diverse as Thomas Piketty, Pope Francis and Barack Obama. It has stimulated international organisations such as the OECD, the ILO and the IMF to turn their analysis as well as policy in new directions. By putting the questions of immigration back into proportion and sidelining those who see these issues only in black and white, the EU – and especially progressive politicians – ought to develop a new focus on the problem of inequality and explore how this would affect its budgetary policies and operations.

The new political advance must therefore go beyond the introduction of a few new goals and tools into the EU budget. In the area of fake news and hybrid warfare, the EU would also need to invest in communication, including more staff in EU representative offices within the member states. Some new priorities just cannot be attained without more people working on them, and this also calls into question whether any real political advance can be made without breaking the glass ceiling.

Co-legislators should assess the true scale of "old" and "new" challenges facing the EU, such as the need for common defence, migration management, environmental sustainability and the reduction of inequalities within and between member states. They should not lose sight of the major contribution that "old" instruments, suitably modernised, can bring to addressing these challenges.

2.6 POLITICAL ADVANCE: OWN RESOURCES

As leader of an expert group,[13] former EU Commissioner Mario Monti has been working on the question of financing the EU, and one of the 2017 reflection papers also presented related questions and options. Based on this process, new own resources would represent about 12 per cent of the total EU budget, according to the Commission, and could contribute up to EUR 22 billion per year to funding the new priorities. The overall size of these own resources appears to be modest, but the shift is seen as a key factor in making the European Union more focused on common interests and less dependent on national contributions and the "juste retour" logic.

In the new MFF proposal, the basket of new own resources includes:

- 20 per cent of the revenues from the Emissions Trading System;
- a 3 per cent rate applied to the new Common Consolidated Corporate Tax Base (CCCTB) (to be phased in once the necessary legislation has been adopted);
- a national contribution calculated on the amount of non-recycled plastic packaging waste in each member state (EUR 0.80 per kilo).

Previous proposals included the Financial Transaction Tax (FTT), which faced a headwind of opposition from countries such as the United Kingdom and Sweden. The FTT ended up in

12 The value of Erasmus is highlighted by Stanishev (2018): "Erasmus is one of the best ways for today's young people to gain invaluable cultural experiences, educational opportunities, language skills, career options and lifelong friendships."

13 The high-level group on own resources (HLGOR) was established in February 2014 in order to explore and outline more transparent, simple, fair and democratically accountable ways to finance the EU. The group was chaired by former Italian prime minister and EU Commissioner Mario Monti and was composed of members appointed by the European Parliament, the Council and the European Commission.

an inconclusive effort as enhanced cooperation. This is, however, an example of a fiscal tool being an incentive at the same time, and the more successfully it functions as an incentive, the less revenue is generated. The plastic related national contribution would have a similar effect in a different area.

Even if initial revenue from some of these channels were small, they can make a great qualitative difference. For example, a revenue from corporate tax on a CCCTB basis would be minor, but it would open a new chapter by allowing the Commission to start collecting tax, which would be a novelty. No wonder such small instruments can polarise opinion across member states, as well as the political spectrum.

New own resources have great potential to help solve the political conundrum around the post-2020 MFF. However, the endeavour to obtain genuine own resources is often portrayed by EU sceptics as an intention of the self-serving EU bureaucracy to draw more money from European citizens without them even noticing, and thus reducing transparency and accountability. Such concerns have to be taken seriously and even in cases where revenues would flow directly from economic actors to the EU budget without spending some time in national treasuries full accountability has to be guaranteed.

2.7 STRENGTHENING THE SOCIAL DIMENSION: TOWARDS A SOCIAL UNION

The political process of EU integration has been stuck since the defeat of the attempted Constitution (2005) and the recent rise of EU scepticism has fostered a sense of retreat. Indeed, the 2017 White Paper was the first major document that invited stakeholders to discuss scenarios of withdrawal or even split. Nevertheless, this state of uncertainty did not block progress in many areas, such as the development of a digital single market or a partial reform of the Economic and Monetary Union (EMU). The implementation of an Energy Union and a Capital Market Union was going ahead and an EU commissioner was appointed with responsibility for a Security Union. Interestingly, discussions about the need for a Social Union remained marginal, putting social policy into a Cinderella role with regard to EU integration.

All this has happened at a time when the concerns about the social dimension are deeper and more widespread than ever before, and Brexit, the main driver of the MFF debates, should be a warning sign. The fact that the benefits of the single market do not automatically trickle down to disadvantaged regions and social groups played a major role in the 2016 referendum result in the United Kingdom. English people outside metropolitan areas felt disenfranchised politically and economically, while UKIP, reinforced by egocentric Tory politicians, ensured that their frustration is directed towards Brussels instead of London and in particular Westminster. Contrary to UKIP stereotypes, British people have not experienced a "too social" EU, but quite the opposite, thanks to UK governments that have expressly chosen not to take advantage of EU funding instruments. The United Kingdom could have used the European Social Fund (ESF) to help municipalities facing migration pressures but did not. It could also have used the European Globalisation Adjustment Fund (EGF) when major producers were downsizing, but its government decided against it. And the United Kingdom could have used the European Fund for the Most Deprived (now called FEAD) to boost the capacity of its food banks, but it did not do so in order to make sure that the more caring side of the EU did not become visible in Britain. This UK government attitude has strongly contributed to the alienation of many British people from the EU, and eventually to the victory of the Leave vote as well.

Consequently, the real lessons of Brexit actually support progressive arguments about the need for tackling imbalances and inequality collectively in the EU and for stronger common instruments favouring economic, social and territorial cohesion. A progressive political initiative would need to take the bull by the horns and highlight the potential of more traditional policies – although in reformed versions – to tackle the problems generated by globalisation and austerity. This applies to the question of cohesion funding in particular, but also to the social dimension of the CAP.

The main concern with the CAP should not be its size but how it affects redistribution and societal relations within the member states. Out of the total CAP envelope, some 80 per cent goes to 20 per cent of land owners, a category that does not overlap with actual farmers. Simply because land ownership is highly concentrated, the CAP is potentially a very regressive distributional policy. There are answers to these issues that would not risk support for agriculture in general, such as a limit on subsidies or a requirement for co-financing (by member states).

Another unfair element in recent CAP funding has been that landowners in old member states have been receiving more than their peers in new member states, but change has started to happen in the right direction. The effects on inequality should be put under greater scrutiny in the new member states, however, where direct CAP payments can easily end up with non-resident speculators instead of with the rural population itself, which in turn feels ever more distanced from urban prosperity.

Establishing and nurturing instruments that support the social dimension of the European Union has always been a responsibility of progressives. On the other hand, the social dimension of the EU budget often appears to be underestimated. This is perhaps because of the low expectations of the EU in the area of social policy in general, and also because of the bias towards legislative instruments in the EU social policy toolkit. If it is explained where and how EU funding connects with human capital investment within the member states, however, its role and significance can be better understood.

Within national budgets, broadly defined welfare expenditures amount to around 40 per cent of total expenditures. Out of this category, social protection budgets narrowly defined receive about one-third. Needless to say, the EU budget can never rival or centralise these budgetary components. But the social component of the EU budget can and does provide vital contributions to social assistance and social investment programmes within the member states, which also function as incentives for reforming employment and social policies and designing more effective programmes on the ground. In many countries, workforce training largely depends on ESF funding.

The European Pillar of Social Rights rightly identified social divergence as a potentially destructive factor not only at the level of the member states but also for the EU. Following a decade of devastating financial and economic crises, the discussion of cohesion and convergence must be serious and avoid clichés. A genuine assessment is needed about the capacity of instruments in the EU budget to deal with the great imbalances and inequalities in the EU, and what role conditionality can play in strengthening the existing instruments.

2.8 STRENGTHENING THE SOCIAL DIMENSION: UPDATING THE ESF

In the period 2016–2017 the Commission involved member states in an exercise to develop a European Pillar of Social Rights (EPSR). This also created an expectation of more forceful tools for the implementation of the EPSR in (or by) the member states. Alongside social legislation and policy coordination, the EU budget is such a tool. The ESF has a primary responsibility here, although under the Europe 2020 strategy the ERDF contribution to poverty reduction was also explicitly recognised (for example, the potential to address housing problems and tackle homelessness).

When the new ESF proposal was unveiled in May 2018, reference was duly made to the EPSR. With the new MFF a new headline figure was presented for the European Social Fund (ESF), EUR 101.2 billion. This means that, for the next long-term EU budget, the Commission proposes to further strengthen the EU's social dimension with a renewed ESF, the so-called European Social Fund Plus (ESF+). The instrument remains geared to investing in people, ensuring they are equipped with the right skills needed to deal with challenges and changes on the labour market, following up on the EPSR.[14]

The ESF+ is expected to be a more flexible and simple version of the current ESF, but the bigger headline number is actually a product of merging a number of existing funds and programmes.[15] Pooling resources is supposed to allow the EU and member states to provide more integrated and targeted support in response to social problems and labour market developments. The merger allows the EU to boast a higher headline figure for the ESF, at the expense of diminishing visibility for the smaller instruments (and the capacity of the EU to address a wider range of employment and social concerns).

Nevertheless, it is important that the new MFF proposal maintains the principle introduced in the current period: the allocation of the ESF has to be defined at EU level in order to ensure that member state governments, driven by short-term considerations, do not reduce human capital investment. In the current period, this function was implemented by an EU-wide minimum share within Cohesion Policy (23.1 per cent), while post-2020 it would be an absolute number that exceeds EUR 100 billion.

On the other hand, the Commission also confirms that within the ESF a defined threshold should protect expenditures related to social integration. In order to ensure that the ESF serves not only the labour market but also the fight against poverty and social exclusion within the member states, the threshold would increase from the current 20 per cent to 30 per cent. Political attention is required not only when the size of such an envelope is defined, however, but also with regard to how programmes are designed, implemented and audited. In many instances money has been allocated for an important social objective, such as Roma integration, but subsequently it proved difficult to trace where the funds actually went.[16]

Similarly to the social integration threshold, the MFF proposal defines a 10 per cent minimum for funding youth employment, although this applies only to countries in which the youth unemployment rate is excessively high. This is a step back from the approach taken in the current period and not only because of the abolition of the separate Youth Employment Initiative (YEI). Following the 2013 Council Recommendation, all EU countries had to implement a Youth Guarantee, which was supported with extra funding in regions in which the youth unemployment rate was excessively high in a particular crisis period. In the future, if a country has no excessive average youth unemployment rate, it would not fall under the minimum spending obligation even if in some of its regions the number of unemployed or inactive youth is high (Sweden or Belgium would be good examples). Secondly, the fact that more is spent on youth employment but without an explicit link to an agreed EU policy and quality standard (Youth Guarantee) means that the results are not obvious. There is certainly a temptation to take a lighter approach at present when the EU economy is not in a crisis, but because the youth employment situation is still far from perfect and will certainly get worse in the next recession, conditioning EU funding for youth employment on the implementation of the Youth Guarantee would be logical in a budget oriented towards results.

What should be more important than the higher headline figure and the orchestration of the general framework is the mission of the ESF and the need to update it. Social imbalances and divergence featured as a major concern at the time of the crisis and afterwards. The potential of EU tools to improve social sustainability should be at the heart of the MFF debates.

Due to the combined effect of globalisation, EU enlargements and the euro-zone crisis, more peripheral countries and regions in the EU have experienced very significant outflows of working-age men and women, resulting in skills shortages, population decline and rapidly increasing old-age dependency ratios. Whether structural or cyclical reasons are more important in driving these trends, the resulting intra-EU imbalances

14 On the occasion of adopting the new ESF proposal, Commissioner for Employment, Social Affairs, Skills and Labour Mobility Marianne Thyssen said: "Europe wants to empower people. We put our money where our mouth is. Our new, flexible and simplified social funds are focused on investing in people: to make sure they have the right skills, to make sure they have modern social protection adapted to new forms of work, and to show solidarity with those who need it most." Highlighting social protection in an ESF context is clearly an impact of the EPSR.

15 The European Social Fund (ESF) and the Youth Employment Initiative (YEI), the Fund for European Aid to the Most Deprived (FEAD), the EU Programme for Employment and Social Innovation (EaSI) and the EU Health Programme.

16 See A roma integráció jelenleg "halott ügy" [Roma integration currently moribund], https://444hu/2017/07/04/a-roma-integracio-jelenleg-halott-ugy

will not go away quickly, and may even be aggravated in the coming period, further weakening the growth potential of the peripheries. These imbalances require a fresh and serious analysis, but also more forceful and better focused investment strategies. It should be an explicit goal of the ESF to promote social investment states,[17] especially on the (Eastern and Southern) peripheries of the European Union, in order to counter divergence and facilitate upward convergence. These concerns and proposals should be elevated higher on the progressive political agenda.

POLITICAL ADVICE AND PROPOSALS

- Advocate an increase of the MFF ceilings in view of newly identified common needs and goals.
- Enhance genuine own resources for the EU budget (to replace part of national contributions).
- Support EU funding to boost security and productivity without calling into question core functions of the EU budget, such as cohesion and convergence.
- Pool resources for common defence and more harmonious living with our neighbourhood.
- Strengthen the social dimension of the MFF (in qualitative terms, beyond pooling of existing instruments).
- Use the example of the MacDougall Report for an inquiry into a more robust EU budget.

17 See the classic text by Vandenbroucke, Hemerijck and Palier (2011).

3

THE ECONOMICS OF THE MFF: ALLOCATION, STABILISATION AND GLOBALISATION

Economists of public finance have identified and focus on three key functions of public budgets: allocation, redistribution and stabilisation. The first concerns the provision of public goods and investment priorities, the second concerns the correction of the income distribution by markets and the third concerns the possible reduction or elimination of cyclical fluctuations of economic activity. The EU budget primarily serves the first objective, with modest contributions to the other two. An economic analysis has to scrutinise the continued justification for the allocation function and explore the potential need to adjust the capacity of the other two (redistribution and stabilisation). Global trends and the expected geopolitical environment of the next decade also need to be taken into account.

3.1 BASIC GROWTH MODEL: SINGLE MARKET WITH MODEST REDISTRIBUTION

The existing MFF is fundamentally a budget for the single market. As John Pinder and Simon Usherwood (2007) explained in their book introducing the European Union: "The single market is a positive-sum game. Because it enhances productivity in the economy, there is benefit for most people, whether they take it in the form of consuming more or working less. But alongside the majority who gain, there will be some who lose from opening the markets to new competition; and these may demand compensation for agreeing to participate in new arrangements."

Textbook economic geography explains clearly that economic activity in a large market tends to be clustered around the centre and that transfers to the periphery are necessary to maintain public goods, prevent major divergence in economic potential and keep living standards at an acceptable level. Consequently, redistribution through Cohesion Policy is not a gift but an indispensable pillar of a single market involving diverse countries of uneven levels of development in the European Union.

Of course, an EU budget existed before the single market was established, but in the early period it was fundamentally an agricultural budget, supporting an area in which the common market and policy were the most advanced. The Single European Act proposed by Commission President Jacques Delors in 1986 contained an article on "economic and social cohesion" and thus Delors proposed a doubling of the endowment of the structural funds. This strengthened the link between allocations and regional income levels, which was most appropriate at a time when the Community welcomed new members in the South: Greece, Portugal and Spain.

With the creation of the EU single market in the early 1990s, a comprehensive Cohesion Policy was developed out of existing and new instruments in order to address existing and potential imbalances, and the risk of uneven economic and social development. The larger and more heterogeneous the EU became after a succession of enlargements, the more vital it became to have a robust and sophisticated system of budgetary instruments supporting cohesion and convergence. This is a crucial part of overall economic performance, but also of political legitimacy in the EU.

Cohesion Policy is supposed to facilitate growth in less prosperous geographical areas. In lower income regions and countries, Community support for investment has to produce not only higher growth rates but also a transformational effect, that is, signs of development that would facilitate growth with less external support at a later stage. These tools and effects of the EU budget are widely publicised, even if the actual redistributive effect of the EU budget as a whole is relatively modest, and mainly supported by the revenue side as opposed to the expenditure[18] side (Pasimeni and Riso 2016).

According to the latest Cohesion Report (published in April 2017), one-sixth of the EU population lives in regions with income levels less than half of the EU average. Most of these regions can be found on the Eastern and Southern peripheries. Even with European Structural and Investment Funds (ESIF)

18 The EU budget is somewhat redistributive primarily because higher income countries contribute more (revenue side). On the expenditure side, only one policy is tuned to redistribution, namely Cohesion Policy, half of whose resources go to regions with below 75 per cent of EU average income. Cohesion Policy spends slightly over one-third of the EU budget and its main components, the ERDF and the ESF, support all member states, including the richest ones.

support, they have stagnated economically and are experiencing demographic decline, generating further imbalances. This means that any serious talk about Social Europe would also need to advocate a higher degree of redistribution, coupled with improved functioning of the tools that serve this purpose.

Markets tend not to equalise but to polarise. In order to prevent divergence in the single market, it needs to have a strong social dimension, in the form of social legislation, support for investment in the less developed countries and regions, and representation of the social partners in EU level decision-making on all issues that affect them. These elements are absolutely fundamental components of the legitimacy of an overall public support for the European project, and the single market in particular. Without the budgetary pillar, the other components would not be able to reconcile the functioning of transnational markets with political and social goals. Solidarity must be material, which calls for reinforcement rather than marginalisation of Cohesion Policy (Jouen 2017).

3.2 ADVANCED GROWTH MODEL: SHIFTING ALLOCATION PRIORITIES

While Cohesion Policy is a place-based growth policy, the EU budget also promotes growth by allocating money to investment priorities, including sectoral choices. Agriculture was an early priority, reflecting the post-war need for food security and a longer-term commitment to preserving rural communities and farm incomes. But the added value of EU cooperation and fiscal capacity was gradually discovered in other fields as well. The EU has funded some mega-projects[19] that individual member states could not have implemented separately, and over time the EU and its budget became the main player in funding research and innovation in Europe.

Becoming a knowledge-based economy has been a manifest EU ambition for two decades, thanks in particular to the Lisbon Strategy (2000). After ten years, this was followed up by the Europe 2020 strategy, aiming at smart, sustainable and inclusive growth, launching flagship initiatives such as the Digital Agenda and the Innovation Union, and including a headline target to increase the research and development expenditure of the member states to 3 per cent of GDP by 2020. At a time of economic recession and austerity, however, most member states have found it very difficult to adjust their budgetary allocations in the right direction. A game changer would be if the EU itself were to shift and also to bring to bear better coordination, including for exploiting synergies and avoiding duplications.

In order to explore the EU's potential for funding and coordinating research and innovation, former Commissioner Pascal Lamy was invited to chair a group, which delivered a report on the matter. Unsurprisingly, Lamy proposed[20] a major increase, ideally a doubling, of EU spending in this area. Horizon 2020, which is the main budgetary vehicle of this EU policy, is already one of the largest global funds for science and innovation in the world (and the largest under a single political authority). Its wide profile, covering curiosity-driven frontier science, support for start-ups as well as partnerships with industry, is a strength.

Lamy and his sponsor Commissioner Carlos Moedas did not only lobby for more money, however, but also advocate a new business model for the EU. This concept is summed up by the draft strategic recommendations outlined by Professor Mariana Mazzucato (2018). This builds on Mazzucato's earlier work, which inquired into how the innovation economy functions in the United States, and pursues a triple objective of smart innovation-led growth, inclusion and sustainability.

Mazzucato argues that Europe can achieve the big leap forward to a competitive, knowledge and innovation-based economy if it takes advantage of economies of scale at EU level and applies a mission-oriented approach[21] (examples of such missions: having 100 carbon neutral cities by 2030, a plastic free ocean, or decreasing the burden of dementia). What is at stake is Europe's relative position vis-à-vis the United States and China in the global economy. For older students of the EU, this also means a shift of focus from negative integration to positive integration, especially in an area so critical for economic progress. Boosting the fiscal capacity of the EU in research and innovation is a key component of a new business model.

Indeed, the European Union should move towards the model of the "entrepreneurial state" à la Mazzucato, as long as it can also ensure that it draws talent for this joint enterprise from all corners of the EU and also shares the benefits fairly. Again, pitting new against old artificially would not deliver this outcome. The full policy chain of investing in human capital, financing research and innovation, and balanced growth has to be worked out. The place-based approach of Cohesion Policy cannot be pushed back by research and innovation until the geographical implications of the second, including the selection and choices of referees and the data on participating actors, are better understood.

19 The most important example is Galileo, which is the European Union's Global Navigation Satellite System (GNSS). It provides accurate positioning and timing information. The long-term and vast investment required by Galileo has often been a target of the UK tabloid press, but now access to Galileo and UK tech transfer to the project is a sticking point in the Brexit negotiations.

20 Pascal Lamy: "Our mandate was not about the budget allocation game. But we are making the case for a much more resourceful programme. Our proposal is to double "FP9" from the current EUR 77 billion programme known as Horizon 2020. EUR 120 billion would be a bare minimum for the next programme. This is a big increase, but I believe it's necessary with where the world is going". See: Gillman (2017).

21 Mariana Mazzucato: "A mission-driven approach can be critical for European competitiveness. Other major players in the global economy, like China or the United States, have innovation systems that are more centralised or focused on a reduced number of key clusters. Europe, on the other hand, is both more fragmented – which can be a negative in terms of gaining scale – and more diverse – which creates a messier but also potentially more creative environment. To capitalise on this asset, Europe needs to take the next step and take advantage of its unique nature as a common market of diverse economies."

3.3 THE NEW GLOBAL ECONOMY: THE COSTS OF DISRUPTION

Uneven economic development matters both inside and outside the EU. Changes in the international division of labour can be a challenge for nations, but also for regions and working communities.

Globalisation has long been considered an opportunity for European business but specific risks have also been identified. The EU has traditionally been a strong advocate of open markets, with the Commission regularly highlighting their positive contribution to EU citizens' prosperity. Even in the context of the revival of US protectionism and unilateralism in recent years, the EU has remained committed to the international trade order and the framework of the World Trade Organization (WTO). As the financial and economic crisis triggered high levels of inequality and unemployment, however, perceptions of free trade have shifted in the EU, with citizens increasingly casting doubt on its economic benefits.[22]

Acknowledging this, the Commission's narrative on trade has evolved. Recent publications recognise that the aggregate benefits of free trade also come with distributional effects. Thus, the 2017 "Harnessing Globalisation" reflection paper clearly states that "there is a risk that globalisation would (…) contribute to further widening inequalities and social polarization".[23] A new EU-level narrative has so far failed to materialise, however, as the assumption is that action in this area is a responsibility of national governments. The proclamation of the European Pillar of Social Rights refers to the impact of globalisation, but its stated principles need to be backed by sufficient financial resources at both national and EU levels.

There is, however, a risk that in the absence of a more pro-active EU agenda addressing the downside of globalisation, heightened pressure on policymakers to close their borders could backfire on the European integration project itself. Such a "populist backlash" would encompass two major threats for the EU. First, progressive economic fragmentation. New barriers across the EU and vis-à-vis the rest of the world would negatively impact Europe's overall prosperity. Second, political disintegration. As Brexit has highlighted, the perceived inability of the EU to address global trends – such as deindustrialisation or migration flows – may suffice to jeopardise the whole EU integration project.

Although endowed with a more limited budgetary capacity, the EU also has a dedicated instrument to deal with the adverse consequences of globalisation: the European Globalisation Adjustment Fund (EGF). Between 2007 and 2016, the EGF supported 140,000 redundant workers and assisted 3,000 young people in finding a job in regions with high youth unemployment rates.[24] The use of the EGF has been limited, however, as national governments have been reluctant to make use of the EU funds available.

According to the new MFF proposal, the EGF will be revised so that it can intervene more effectively to support workers who have lost their jobs. Currently, workers can get support from the Fund only when their dismissals are due to changing trade patterns or consequences of the financial and economic crisis. Under the new rules, other reasons for restructuring, such as automation, digitalisation and more, can be eligible for support, taking account of new challenges on the labour market. The new rules will also lower the threshold of workers dismissed for a case to be eligible from 500 to 250, which will allow more workers to get support. For seven years, the EGF would be allowed to spend a total of EUR 1.6 billion.

The Commission's proposals will probably ensure that the small framework of the EGF is better exploited. It would also be important, however, to better assess the distributional impact of trade deals and establish the areas in which EU spending could effectively help address the roots of people's concerns about globalisation. More concrete proposals could follow to support European governments in dealing with the distributive impact of industrial transformations, develop robust social buffers to deal with external shocks or respond to protection needs over the life course, besides specific restructuring operations. These proposals would require the EU to consider a response to globalisation that goes well beyond enhancing competitiveness.

3.4 THE NEW GLOBAL ECONOMY: THE SUSTAINABILITY IMPERATIVE

Ecological and environmental sustainability is a key question in today's global economy and Europe has been leading the analysis as well as action to address the relevant challenges. In the past decade, climate policy and the protection of the environment have been central issues on the EU policy agenda. Sustainability is one of the three pillars of the Europe 2020 strategy. In the 2010–2014 period one of the 27 (later 28) commissioners was responsible for climate change and the related global negotiations. Subsequently, climate issues were merged with the energy portfolio, just as the environment was merged with maritime and fisheries. (To compensate for these losses, one of the vice-presidents was given the task of supervising sustainability as part of his extra-large pile of dossiers.)

The sustainability agenda has been one of the factors shaping the MFF. Greening has been the main factor in the reform of the CAP and the Blue Growth strategy[25] has been the dominant theme in the programming of EMFF in the current period. These strategies did not induce more allocations, but helped to avoid sharp cuts in the CAP and the EMFF, and

22 A 2016 survey by the Bertelsmann Foundation conducted in Germany found that there has been a "clear decrease in the fundamentally positive opinion of trade": https://www.bertelsmann-stiftung.de/fileadmin/files/BSt/Publikationen/GrauePublikationen/NW_Attitudes_global_trade_and_TTIP.pdf

23 European Commission, "Reflection Paper on Harnessing Globalisation", May 2017, Brussels, https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-globalisation_en.pdf

24 With a record of around 50 per cent of workers finding a new job, the EGF has also shown a high rate of success, especially taking into account that the workers targeted were often lower-skilled and disadvantaged jobseekers.

25 Blue Growth is the long-term EU strategy to support sustainable growth in the marine and maritime sectors (aquaculture, coastal tourism, marine biotechnology, ocean energy, seabed mining), driven by the understanding that seas and oceans are drivers for the European economy and have great potential for innovation and growth. Blue Growth is the maritime contribution to achieving the goals of Europe 2020.

allowed the EU to contribute to global public goods beyond its own borders.

Recent years have seen further progress internationally with the conclusion of a global agreement, the Paris Accord, on climate protection. The social and political implications of the related strategies have also become better understood. Further discussions[26] and policy decisions are in the pipeline, suggesting that in some areas the EU itself has to be more ambitious. A more radical decarbonisation path is expected to be defined in the upcoming EU mid-century zero-carbon roadmap, due in early 2019.

In view of these plans and expectations, and because of the expected impact on employment, trade unions have been highlighting the need for adequate funding for a "just transition". Because it has often been found that climate action risks adverse social outcomes (for example, climate-related taxes may put a heavier burden on poorer people), relevant studies have to be carried out urgently and tools, including budgetary ones, need to be found to tackle risks and manage transformations.

A just transition should be an integral part of a broader low-carbon strategy and, to connect with social partner demands, the EU could set out its own just transition framework and roadmap, based on the relevant ILO guidelines but adapted to the specific challenges in the European context. Because this international dialogue is taking place in parallel with the EU MFF discussions, the participants in our discussion must keep an open mind and prepare for corrections or even new proposals, depending on the policy process.

In this search for effective strategies and appropriate tools, the idea of giving the EGF a leading role in tackling the employment effects of decarbonisation has been floated. The need for additional funding for the "just transition" is beyond doubt. What is not obvious is that the EGF would be best suited to deliver this function. The EGF has been a fund with the capacity to respond to "micro-shocks" that cannot be handled by local authorities and stakeholders alone, especially at a time of strict fiscal constraints. On the other hand, climate change is neither micro nor a sudden shock but a factor that requires long-term adjustment in a consistent and coordinated fashion. In this particular case, the value added of EU coordination and funding is that it can keep policies as well as budgetary resources stable over political and economic cycles. A strong Cohesion Policy, assigned with a "just transition" as one of its key post-2020 objectives, would seem to be a more logical choice.

3.5 EMU FISCAL CAPACITY AND STABILISATION FUNCTION

Today we are speaking not only about maintaining and improving the conventional budget framework of the EU and its single market but also an embryonic budget for the eurozone as well. While for a long time after Maastricht the belief prevailed that monetary union can happen without fiscal union, the post-2008 crisis broke this taboo. The 2012 Four Presidents' Report concluded that to avoid a disintegration of the EMU major steps towards a Banking Union, Fiscal Union and Political Union were needed, within the foreseeable future.

The strong showing of various nationalist and anti-EU forces at the 2014 EP elections and in various member states, however, have put the possibility of a shift towards fiscal union in doubt. The new Commission partly absorbed the EU sceptic views and the reform of the EMU took the track of further analysis, reflection and proxies. Nevertheless, the 2017 presidential elections in France have opened a new horizon, and even from Germany some encouraging voices are occasionally heard. Slowly, slowly it is becoming understood that certain functions (cross-country risk sharing and counter-cyclical stabilisation) can be performed only through fiscal instruments in a monetary union, and those functions should not be mixed with the budget of the whole EU, or the operations of the central bank. If we have more objectives we need more instruments as well.

Guntram Wolff (2017) argues that out of the three key functions of public finance (allocation, redistribution and stabilisation) it is primarily stabilisation that provides a rationale for the debate on the euro-zone budget. Because Brexit would reduce the gap between the EU and the euro area, however, it becomes questionable whether a separate budget should be aimed at with such a temporary character (for the few years until the outstanding countries manage to join). The counter-cyclical potential in the existing EU budget remains very small, however. David Rinaldi and Jorge Núñez Ferrer (2017) identify no more than three tiny instruments (YEI, EGF, EUSF) with a profile linked to shock-absorption. Manipulation of co-financing rates can also be added to the modes list of counter-cyclical measures at the time of the recent crisis.

Thus building a proper fiscal capacity for the euro-zone is of vital importance. It is possible without a federal leap or a treaty change. The key requirement is that political leaders be able to convince the public also in the surplus countries of the necessity of repairing the EMU and preparing it for the next downturn, including by adding shock-absorption tools. This is a function very different from the original and still standard mandate of Cohesion Policy, however, which is meant to address structural gaps and discrepancies rather than cyclical fluctuations.

One should note that, in terms of receipts, Greece would become a "winner" of the new MFF proposal by a significant increase of net flows as compared with the previous period. Some might say this would be fair compensation for the losses the country suffered at the time of the crisis and evidence of the EU being responsive. But from the point of view of economics, making this connection is flawed, because Greece has suffered primarily because of the lack of adequate cyclical (more precisely: counter-cyclical) policies and fiscal tools, and delayed support for infrastructure development and other structural causes is not the right answer. With adequate cyclical tools in place, Greece would not have suffered losses of this magnitude. Providing more resources for investment ex post is the right action in the current circumstances, but not a substitute for repairing the system and building a fiscal capacity tailored to the needs of the Monetary Union.

26 Most importantly, the 24th UNFCCC meeting in Katowice in December 2018.

3.6 EMU FISCAL CAPACITY: WHAT IS ON THE TABLE

Following new calls for a fiscal capacity, including from the European Parliament and the newly elected French President Emmanuel Macron, the Commission President in his State of the Union speech announced that a budget line dedicated to the euro-zone would be embedded in the next MFF proposal. Although previously new requests and suggestions were linked to the euro-zone with its current composition, this solution is consistent with the fact that the euro is defined in the Treaty as the currency of the whole European Union. On this ground, calls for a euro-zone parliament have also been rejected because the European Parliament is competent on all related matters.

At the same time, the Commission voiced its intention to reunite the EU and the euro-zone which, after Brexit, faces fewer hurdles, given that out of all non-euro-zone countries only Denmark[27] has no obligation to introduce the single currency as soon as the criteria are met. Thus the point is not so much that the proposed euro-zone budget is embedded in the MFF, but what concrete tools are being put forward and how they would work.

In the MFF proposal, the euro-zone compartment includes two new items:

– a Reform Support Programme (RSP) with EUR 25 billion;
– a European Investment Stabilisation Function (EISF) with EUR 30 billion.

The RSP, apart from offering a Reform Delivery Tool and technical assistance, also introduces a Convergence Facility to provide dedicated support to member states seeking to adopt the euro.

But what exactly is the nature of these new instruments? To start with the RSP, it is being designed to support structural reforms in the member states in line with recommendations outlined in the context of the European Semester. The benefits and functions of such an instrument are not obvious, for several reasons. First of all, a monetary union justifies fiscal tools that are more cyclical than structural. Events that trigger fiscal support require urgent treatment and cannot wait for the next round of Country Specific Recommendations (CSRs). On the other hand, the previous round of CSRs may not be relevant to the new situation, should a financial crisis occur in the autumn (which is normally the case). Second, there is a practical difficulty in calibrating structural reforms. How can one design a menu of reform actions and related envelopes that would apply even-handedly from Finland to Portugal, and from Ireland to Bulgaria? Even more importantly, the content of the support programmes also has to be scrutinised. If such programmes merely serve the purpose of internal devaluation, it could be more controversial and counter-productive than helpful. Overall, the RSP seems to revive an old (and failed) idea that was on the table of the European Council in 2012–2013, namely the Competitiveness and Convergence Instrument (CCI). It was discarded because of concerns very similar to those listed above. The RSP appears to be at best an attempt at political fudge, promoted by those who fear that economically sounder instruments might be impossible to agree politically. A harsher assessment would be that the RSP is a hobbyhorse of people who have learned nothing and forgotten nothing from the crisis experience. A combination of a robust Cohesion Policy and new instruments for counter-cyclical stabilisation would be a superior solution.

The second newly proposed tool, the EISF, is supposed to maintain the continuity of investment projects in times of crisis. This is not a source for transfers, however, but loans in order to compensate for interest rates potentially being hiked in a turbulent period. This tool would indeed serve a useful purpose, but at this stage there are still question marks around it. In case of a major crisis, it is not unnatural to reprogramme investment projects and this also takes time. This may cause delays while support arrives from the EU level. Besides, the crisis also means that some economic actors may be transformed or even disappear in the meantime, which would cause further complications. Importantly, support from this facility would be focused on a particular project, which probably means that the effect would be local, or at least territorially concentrated. The EISF could thus provide asymmetric support in times of asymmetric shock and may result in a situation in which large parts of a country and its population remained uncovered. One way to mitigate this risk would be to modulate the EISF in such a way as to include general budget support that could also be used to co-finance country-wide social investments, such as teachers' salaries.

After the Commission unveiled these fiscal tools integrated into the new MFF, the small size and somewhat bogus nature of these instruments invited Financial Times columnist Wolfgang Münchau to call the approach "homeopathic". This might be a pertinent description, but even so the discussion of these token instruments allows a new round of discussion about stabilisation in the euro-zone. There are surely multiple options to resolve this problem. One can opt for a new stabilisation facility that is comparable in size to the existing EU budget, or for a significant relaxation of the fiscal rules. Further innovative action, albeit intransparent, inside the European Central Bank is also possible. One of these directions has to be chosen before it is too late, however. Budgetary solutions have the advantage of being rule-based, targeted, transparent and involving political accountability, as long as they are appropriately designed.

3.7 EMU FISCAL CAPACITY: DEMAND AND REVENUE SIDES

If there is consensus about the need for an EMU fiscal capacity and to embed it in the MFF with a stabilisation function, it is important to ensure that such an instrument allows for demand-side intervention, can step in without major delays and can reach a large number of citizens affected by adverse macroeconomic developments. Unemployment insurance, or reinsurance, satisfies these criteria. This is why progressive

27 Ironically, Denmark, which has the right to keep its national currency forever, is closer to the euro-zone from an economic point of view than some other non-euro-zone countries that maintain floating currencies and inflation targeting regimes, such as Sweden or Poland.

thinkers and leaders[28] have been advocating this for some time.

A Community unemployment fund is not entirely a new idea. It was first outlined by the 1975 Marjolin Report and supported by the 1977 MacDougall Report[29] as well. Those early documents of public finance analysis considered it a no-brainer that monetary integration requires unemployment insurance as a form of de facto solidarity. Since the euro-zone crisis of 2011–2013, a great deal of analysis, including by the Commission itself, as well as a host of think tanks and independent experts, has explored the case and run simulations, all pointing overwhelmingly to economic and social benefits.

Various models have been put forward, including partial pooling of unemployment benefit schemes (Sebastian Dullien) or the reinsurance of national unemployment funds (Daniel Gros). Had either of these insurance mechanisms existed in EMU from the start of the single currency, all member states would have been beneficiaries for shorter or longer periods. Countries experiencing a severe recession would have received fiscal transfers, helping them towards a faster recovery and avoiding a perception that, for the EU, arbitrary fiscal targets are more important than democracy and social cohesion.

Irrespective of which model is eventually chosen, euro-zone unemployment insurance can deliver stabilisation in three ways. First, they would contribute to economic stabilisation by shifting demand and purchasing power to countries and regions that would otherwise need to implement fiscal "adjustment" and internal devaluation. Second, social stabilisation would be enacted as well by directing the flow of funds towards more vulnerable groups and helping to tame the rise of poverty among the working age population (which has been a major trend in recent years in Europe). The third type is institutional stabilisation. EMU is based on rules but their application has been the subject of academic as well as political debates. Member states agreed to tighten them but pragmatic considerations often point towards more flexibility, the cases of Spain and Portugal furnishing the latest controversy. While some experts simply recommend ignoring the rules and giving up on them entirely, it is more likely that a modus vivendi could be found through the creation of stabilisation tools that would allow the reconciliation of uniform fiscal rules with the need to maintain national welfare safety nets and social investment capacities.

The funding of an EMU unemployment insurance is a further question, although if the fund is embedded in the MFF, the issue is somewhat simplified. Neither model is tied to one or another specific form of funding. There are many ways of combining sources, even if the fund is embedded. When building the scheme in practice, one of the most important questions that has to be answered, and ideally at the very start, is whether the fund would be allowed to borrow or not. Allowing it to borrow would help to maximise its stabilisation impact (adding an inter-temporal dimension to the inter-regional one).

The small size of the proposed EU budget makes it necessary to explore whether the revenue side can also help the stabilisation function. For example, a small levy on current account surpluses would be very logical. The EU has been pointing to excessive current account surpluses as destabilising factors since 2010, under the Macroeconomic Imbalances Procedure[30] (MIP), but no appeal has been effective. The MFF provides an opportunity to give bite to the rule that requires surplus countries to increase investment and wages and thus boost aggregate demand to help not only themselves but also the whole Community.

If it is now or never for a euro-zone fiscal capacity, this issue can hold back the entire MFF debate. In the absence of orderly fiscal transfers and transparent incentives, the monetary union could collapse. And if the current budget debate leads to a harsh reduction of investment resources by cutting ESIF, the single market could also disintegrate. The stakes are high and the sooner the member states stop playing chicken the better, especially if they take the one-year time frame for MFF negotiations seriously.

ECONOMIC ADVICE AND PROPOSALS

- Maintain the MFF allocation functions (and invest in improving their delivery capacity).
- Double the funding of research and innovation to change the European business model.
- Establish a proper euro-zone stabilisation capacity, if possible with a focus on fluctuations of unemployment.
- Introduce a modest levy on current account surpluses as another form of EU own resource.
- Enhance EU fiscal capacity to deal with globalisation effects and climate change.

28 Italian finance minister Pier Carlo Padoan (2014–2018) has been campaigning for an unemployment insurance fund embedded in the MFF, and more recently German finance minister Olaf Scholz came out in favour of a similar idea, though on the basis of loans rather than grants, which presents a more symbolic rather than substantial version of solidarity. For a concise economic argument on this issue see Andor and Pasimeni (2016).

29 While distant in time from the actual introduction of the single currency, the MacDougall Report highlighted this important link with the following argument: "Apart from the political attractions of bringing the individual citizen into direct contact with the Community, it would have significant redistributive effects and help to cushion temporary setbacks in particular member countries, thereby going a small part of the way towards creating a situation in which monetary union could be sustained."

30 The MIP widens the scope of macroeconomic surveillance from the narrow focus on annual budget deficits and debt/GDP ratios to various other imbalances that may increase the risk of financial and economic crises. Among other rules, it established a 4 per cent limit for current account deficits and 6 per cent limit for current account surpluses. Germany and the Netherlands have exceeded the limit for a very long time and have taken no effective action to bring down their current account surpluses, which can be interpreted as exporting unemployment to other countries of the Community.

4

THE OPERATION OF THE MFF: KEEPING INSTRUMENTS ON TARGET

Operational questions hardly ever make it to the main table of MFF debates. This is certainly a problem because very often it depends on operational aspects whether the instruments can perform according to expectations or not. Therefore, without going into the discussion of financial management in too much detail, we need to identify some key issues of operation (management, engineering, conditionality and evaluation) that connect with the key political and economic objectives. This will allow us to go beyond criticising the proverbial complexity and rigidity of the EU budget.

4.1 DEFINING PURPOSE AND MEASURING PERFORMANCE

The 2014–2020 MFF was designed to boost the transformational effects of the EU budget, namely by serving the objectives of the Europe 2020 Strategy.[31] The first two headings of the MFF, amounting to about 90 per cent of the budget, reflected the Europe 2020 goals (smart and inclusive growth; sustainable growth; natural resources). Apart from this concrete definition of budget purpose, the post-2014 Cohesion Policy introduced some important novelties, such as the partnership agreements and the code of conduct. A new effort was made to make evaluation "results based", and through a more objective assessment of results to help planning and programming in the following period. GDP per capita remains the main allocation principle (with three categories of region eligible for Structural and Investment Funds), but the performance of funds has not been measured purely by contribution to GDP growth but through their contribution to achieving Europe 2020 targets.

Cohesion Policy[32] in particular has always been about supporting structural transformations while enhancing growth opportunities in more disadvantaged regions in the context of the single market. The evaluation of its contribution has always been difficult, however. Member states are pre-occupied with the speed of absorption, while in the European Parliament the focus often shifts to the "error rate". Judging how much Cohesion Policy instruments actually contribute to growth and its quality is hard because it is not redistribution alone that produces results but other factors, too, such as private investment and access to markets.

Cohesion is what the participants in the Community feel, while convergence is what they can measure. Though imperfect, the most important indicator for measuring convergence in the EU is GDP per capita. In other words, the most important expectation vis-à-vis Cohesion Policy is that it helps less developed member states and regions to higher growth rates and convergence to the average EU income level. Whether cohesion-funded regions experience faster GDP growth than non-assisted regions is a usual basis for judging the effectiveness of this policy (see, for example, Darvas and Wolff (2018)). On the other hand, framing the MFF in the Europe 2020 strategy invites another type of evaluation because the question is whether lower-income regions and countries can also get closer to the Europe 2020 targets or not. Pushing aside the Europe 2020 strategy on the political agenda of the EU makes it harder to evaluate the performance of the budgetary instruments (especially ESIF) and returns us to the imperfect fall-back option of using GDP.

To avoid leaving the purpose of EU funds void, reference is often made to the UN Sustainable Development Goals (SDGs), as well as to the European Semester. Neither solution is problem-free. The SDGs, for the time being, lack a particular European focus, and also the political standing that would be required. This can change but not quickly enough to have a meaningful impact on the ongoing MFF negotiations between member states and political forces.

31 The Europe 2020 Strategy was adopted by the European Council in 2010 as a replacement for the earlier Lisbon Strategy in order to achieve "smart, sustainable and inclusive growth". Europe 2020 was articulated in terms of seven "flagship initiatives" and supplemented with five headline targets. Member states were asked to develop their own Europe 2020 plans in order to reach their own targets, and the European Semester was used to monitor progress and provide guidance to help the implementation.

32 Here we are talking about three instruments: the Cohesion Fund (CF), the European Regional Development Fund (ERDF) and the European Social Fund (ESF). Together they represent over one-third of total MFF resources.

The European Semester is EU-specific and politically a strong tool, but there are widely differing opinions about whether it works at all. To some extent, there is a time inconsistency as well because without Europe 2020 or another long-term strategy, it becomes an annual exercise, while EU funding requires a stable and longer-term framework. In order to accept a strong link between EU funds and the Semester it needs to be defined what longer-term strategic purpose is served by the latter. Regarding legal basis, the Semester is linked to the Broad Economic Policy Guidelines and the Employment Guidelines, and institutionally it is owned by DGs ECFIN and EMPL in the Commission and ECOFIN and EPSCO in the Council. Cohesion Policy and its institutional owners, such as DG REGIO, find themselves in a subordinate position, which is a matter for political judgement and decision-making.

4.2 SIMPLIFICATION AND FLEXIBILITY: MIRAGE OR OPPORTUNITY?

A widespread criticism of EU funding is that the system is too complicated and bureaucratic, which also results in excessive rigidity. In general, the EU is often portrayed as an excessively bureaucratic organisation (as opposed to national governments), triggering constant criticism of perceived performance and the assumed lifestyle of "Eurocrats". What follows from this view are constant calls for simplification[33] and greater flexibility, which appear to be the most obvious demands in the context of EU budget reform.

Simplification is a key demand from beneficiaries or potential beneficiaries of structural and investment funds. Applications are deemed too bureaucratic and in fact the system has fed a veritable industry that otherwise would not exist. Even if beneficiaries learn fast and become more experienced with time, this "EU funds business" will remain in operation unless a major reform can be implemented. A cry for simplification was also heard in the previous MFF planning period and was answered, for example, by creating a single regulatory framework for all the structural and investment funds. The creation of the Common Provision Regulation (CPR) for the current funding period represents a simplification for stakeholders because it makes it easier to administer[34] EU funds within member states, but also in Brussels and Luxembourg. Similarly, administration has been made easier with the introduction of simplified cost options, and planning became less complicated with the possibility of "multifund" programmes.

Simplification, however, can often be just a call for easier access to taxpayers' money without the need to comply with common rules and policies. For example, a current proposal to simplify the CAP aims at giving the member states more leeway in deciding on priorities as well as operational details. This would dilute, if not undo completely the previous policy for the "greening" of the CAP, which aimed at reconciling it with environmental objectives and, equally importantly, helped to defend the established size of the envelope. If the new proposals are accepted under the umbrella of a simplification drive, access to agricultural funds will be easier, but at the same time the added value of an EU level agricultural policy is likely to be reduced. Simplification, in other words, becomes a code word for "renationalisation", more or less.

Similarly, flexibility can have various meanings. It is a demand often connected with the MFF's unusually long timeframe It is of course fair to claim that planning for seven years is not easy. Conditions may change after the planning period, and too many rules and rigidity prevent governments at various levels from responding adequately to a new situation. This concern can be addressed eventually by reducing the time frame (for example, from seven to five years[35]), or allowing for a review at half-time or just for the last two years. Another form of flexibility is provided by performance reserves that, under the condition of quality implementation in the core period, allow for greater freedom as regards extra time. Flexibility in public finance can also be linked to the capacity to borrow and thus deal with intertemporal challenges.

4.3 SIMPLIFICATION AND FLEXIBILITY: THE COSTS OF BUREAUCRACY

When options with regard to economies in the EU budget are considered, it is not only the largest chapters that come under scrutiny but the operation of the EU institutions itself. Does the EU have too many bureaucrats? Has the proliferation of EU agencies gone too far and should it not be reversed? Are those in Brussels not paid too much, enjoy fabulous benefits and spend taxpayers' money without proper control? Could the EU reduce the 6 per cent share of expenditures that the EU spends on its own institutions?

Such concerns can surround any central bureaucracy, not only the European one and, as in other cases, it is important also in the EU context to separate myth from reality. For example, it is a stereotype, if not a myth, that fraud with EU funds costs a lot for the EU and, indirectly, for taxpayers. In reality, most of the controversies surrounding EU funds represent irregularities rather than fraud, and the majority of irregularities take place within the member states, and not in Brussels. Most of the irregularities found are considered to be administrative mistakes with no intention of fraud, but of course it is true that all sides could do more to avoid such mistakes. Altogether, about 0.2 per cent of total EU expenditures are affected by fraud, which is a small percentage but a large sum of money. The EU has to aim for zero tolerance on such matters. Combatting and eliminating fraud is an important task, even if it can only contribute in a modest way to reducing waste.

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33 Stanishev (2018) provides an example of a programme (Erasmus) becoming more accessible and thus increasing its chances of achieving the declared objectives through simplification: "application procedures must be simplified and made more user-friendly. Administrative barriers to entry must be removed, especially when it comes to recognition, ensuring that employers and educational institutions across Europe recognise the value of a period spent studying or working in another country".

34 Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laid down common provisions on the European Regional Development Fund (ERDF), the European Social Fund (ESF), the Cohesion Fund (CF), the European Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF) and it also repealed Council Regulation (EC) No 1083/2006.

35 A transition to a five-year duration for the MFF was recommended by the report by Olbrycht and Thomas for the European Parliament.

Another concern, and a seasonal hot topic for the tabloid press in some countries, is the level of salaries in EU institutions. Having EU salaries higher than national salaries in most member states follows the logic of international organisations. Attracting the best is just one point that has to be recognised; others include the international nature of changing jobs and homes. In most cases, at least temporarily, spouses give up their jobs due to international relocation, and one salary is supposed to support the whole family. To some extent, EU jobs also compete with the private sector, in which earnings can be significantly higher. Defying these factors is indeed a possibility, but it would increase the risk of having a smaller pool of candidates in the competition for EU jobs or risk a fall in the quality of applicants.

While explaining the compelling logic for the maintenance of good remuneration for EU staff, it has to be stressed that the legitimacy of this system depends on a strong record of meritocratic selection and promotion. Any case of favouritism or bypassing the rules and standards for the sake of personal or political reasons damages the reputation of the institutions and support for the EU as a whole.

The biggest item of expenditure that cannot be explained on the grounds of economic rationality is the location of one of the seats of the European Parliament in Strasbourg and the monthly meetings of both Parliament and Commission in the Alsace city on the Rhine. This is purely a matter of political symbolism, but as such it is protected by the Treaty. According to many MEPs, maintaining Strasbourg is not only a waste of money but also a waste of time. Added to the duplication of buildings and offices come the greater difficulties of travelling to Strasbourg as compared with Brussels, where practically everything can be done that is currently being done in Strasbourg.

Pushing for savings in Brussels and EU agencies across Europe but ignoring the question of Strasbourg makes a weak and inconsistent case for budgetary savings. Because we are talking about political symbolism, however, it is very difficult to attach prices and compare costs. Nevertheless, there have been repeated suggestions about finding a replacement for the European Parliament in Strasbourg that would be economically and politically satisfactory, if not more beneficial, for the city, the region and the French state. For example, installing a permanent European university campus could very well compensate for the loss of MEPs' purchasing power, although perhaps not in the same hotels and restaurants. And, arguably, having one annual meeting of the European Council in Strasbourg would be sufficient to keep the city and its history in the public attention as much as twelve sessions of the European Parliament. The irony, of course, is that while Strasbourg is a matter of significant budgetary implications, it is not an MFF issue but a matter for Treaty change in the future.

4.4 EMPOWERING THE LOCAL LEVEL

In many cases, calls for simplification and flexibility can be answered by bringing financial instruments closer to the local level. Empowering local actors and making access to EU funding easier for them is a direction that needs to be explored, even if it means from the outset that wherever such steps are made the control of national authorities may weaken. But that is the point, namely that maintaining the full control of national authorities over anything and everything can be a source of complications and delays.

The EGF provides examples of the local level needing EU support but the national level for some reason not applying for the EU fund. To the extent that co-financing is required – and the standard source for that is the national budget – the gate-keeping role of the member state government is understandable. But one might also expect municipal or regional governments to have the fiscal capacity for the necessary co-financing, so the regulations should allow them to apply directly to the EU, without involving the national level.

Another example is capacity-building for the social partners. This important function, in line with the Treaty, which defines the EU as a social market economy, can be performed by tools in shared management but also direct management. The risk of political favouritism, and thus of diverting funds from their true purpose, is much less in the second case. Consequently, it is important to maintain, but if possible also to enhance the capacity of the Commission to directly support social partner organisations and activities in the member states.

Migration management is another area in which the rationale for the empowerment of the local level (cities and regions) is compelling. Gesine Schwan (2018) has advocated a scheme[36] based on the creation of "a European fund which would finance the municipalities which are ready to integrate refugees. As a positive incentive these municipalities should get the same amount of financing for their own development." The assumption is that cities are often more open-minded and pragmatic about immigration and closer to the integration needs and capacities of the economy and society in this respect than national governments, which of course have the main responsibility for border control.

An example of direct contact between Brussels and local actors comes from the recent past, when the Commission launched two pilot programmes: tailored support for the specific challenges of regions[37] facing industrial transition, and interregional innovation partnerships supported by EU funds. The rationale for such innovative programmes was explained by Commissioner for Regional Policy Corina Creţu: "Industrial transition is a major challenge for our economy and society. We need to find new ways to ensure that everyone everywhere can benefit from the opportunities of innovation and technological change."

Cities and NUTS 2 regions have to be empowered and allowed to have more direct links with the EU level, which would also mean a closer connection of the citizens with the Union, countering a trend of alienation. Such solutions would

36 Schwan (2018) aims to replace the stick with the carrot: "There would not be any negative sanctions for national governments not granting access for refugees to their countries. But municipalities in their countries would probably start pushing to have the refugees accepted in order to obtain the financing of their development through the integration of refugees."

37 Regions that have been selected include Cantabria (Spain), Centre-Val de Loire (France), East-North Finland, Grand-Est (France) and Greater Manchester (United Kingdom) as well as Lithuania and Slovenia. See http://europa.eu/rapid/press-release_IP-18-1506_en.htm

also function as a broader encouragement to pursue complex and robust development strategies that can be directly assisted by EU interventions. A general counter-argument against bypassing the national level can be that particular EU funds may come with the need for national co-financing. The local level should feel empowered but it should not be entitled to force the national level to sign blank checks. Co-financing, however, where it applies, should be allowed to come from other resources than the state budget, including promotional banks or the private sector.

4.5 ENGINEERING AND LEVERAGING: FINANCIAL INSTRUMENTS

One approach to EU funding that might help it become more efficient is the development of financial engineering. In the 2005–2006 period, when the MFF for 2007–2013 was designed, "Jaspers", "Jeremie", "Jessica" and "Jasmine" became household names or rather acronyms.[38] After being mere curiosities for a while, this new toolkit turned out to be the first phase of a new period of EU funding.

Financial engineering plays an important role. While admittedly introducing some complications into the lives of the beneficiaries of EU funds, it helps to mobilise funds from beyond the EU budget, including private finance, but by developing financial and technical knowledge it also helps to prepare regions and beneficiaries for a life without grants in case the assisted development effort is successful. When the financial and economic crisis was being tackled (2010), the Progress Microfinance Facility was introduced, which also represented an extension of financial engineering capacity to the social dimension.

In the current MFF (2014–2020), more room has been provided for financial engineering as compared with the previous cycle, when new instruments were introduced. Microfinance was integrated into the EaSI fund. Breaking the uniformity of grant funding in Cohesion Policy was driven by the intention of bridging the gap between public and private funding methods, and helping beneficiaries move from one form to another, as their regions or countries are also expected to make progress (and expect less EU funding in the future).

In other words, every MFF cycle has introduced new types of operation, helped to tailor Cohesion Policy to specific needs and tasks and created alternatives to the conventional method. Another example of departure from Cohesion Policy orthodoxy was the establishment of the Connecting Europe Facility (CEF), which was presented as a key EU funding instrument to promote growth, jobs and competitiveness through targeted infrastructure investment at European level. The CEF supports the development of high performing, sustainable and efficiently interconnected trans-European networks in the fields of transport, energy and digital services. Even if the actual volume for CEF fell short of what was originally proposed by President Barroso in 2011, investments[39] under this umbrella fill missing links in Europe's energy, transport and digital backbone.

Another effort by Barroso to enhance the EU's investment capacity was the call for "project bonds". Shortly after Europe 2020 was launched, it became obvious that achieving what had been agreed would require much larger volumes than what is available at the EU budget. How to leverage much more became the crucial question, and a deep dialogue between the Commission and the EIB began. It took several years until, in 2013, a large offshore submarine gas storage facility in Spain, costing a total of EUR 1.4 billion, signalled the start of the practical implementation of "project bonds". At the time of the financial and economic crisis, the Commission also proposed a capital increase for the EIB, which nevertheless remained concerned about its AAA rating. Eventually this led to the creation of a fiscal cushion provided from the EU budget and produced President Juncker's most emblematic achievement (European Fund for Strategic Investment (EFSI)).

4.6 ENGINEERING AND LEVERAGING: INVESTMENT PLANS BEFORE AND BEYOND 2020

The interest in financial engineering was energised by fiscal constraints at national and EU levels at the time of the recent crisis, resulting in a push for more new financial instruments. The Juncker Plan[40] and the proposal to insert a new tool in the MFF in its wake in order to solve Europe's investment problems bring this process to a new level. In order to form an opinion, we need to look back at the origins of this and its various stages.

Announced at the end of 2014, the operational method[41] of the Juncker Plan represents an important innovation in the system, and has played a role in economic recovery by mobilising finance but also by proposing to exclude member state contributions from national deficit and debt rules. The Juncker Plan also involved downgrading transformational goals (Europe 2020), however, and lacked a social dimension (Huguenot-Noël and Zuleeg 2016). It was not launched as a tool to promote cohesion or convergence, but to encourage

38 JASPERS: Joint Assistance in Supporting Projects in European Regions; JEREMIE: Joint European Resources for Micro to medium Enterprises; JESSICA: Joint European Support for Sustainable Investment in City Areas; JASMINE: Joint Action to Support Micro-finance Institutions in Europe.

39 In addition to grants, the CEF offers financial support to projects through innovative financial instruments, such as guarantees and project bonds. These instruments create significant leverage in their use of the EU budget and act as a catalyst to attract further funding from the private sector and other public sector actors. Through such operations the CEF benefits people across all member states, as it makes travel easier and more sustainable, enhances Europe's energy security while enabling wider use of renewables, and facilitates cross-border interaction between public administrations, businesses and citizens.

40 In July 2014, investment was declared a priority by newly elected Commission President Jean-Claude Juncker. He identified one of the Vice-Presidents as the investment chief of the EU, and presented his investment plan to the European Parliament as early as November 2014.

41 According to the Juncker Plan, the EU provides EUR 16 billion from its own budget, supplemented by an additional EUR 5 billion from the European Investment Bank (EIB). With this seed capital, the European Fund for Strategic Investment (EFSI) hoped to attract almost EUR 300 billion in private sector investment. Member states were also encouraged to contribute. Upgrading of the programme was made dependent on future developments and needs.

the European Investment Bank (EIB) to roll out projects that otherwise would be too risky.

Early critics of the Juncker Plan included Henrik Enderlein and Jean Pisani-Ferry (2015). In their report to the German and French ministers of the economy, they offered a broader concept of investment coordination, more tailored to country-specific situations and policy agendas. They argued that constraints for some member states were more objective and for others more subjective. The EU would therefore need an agreed methodology to channel investment to countries that have performed below potential.

Similarly to Enderlein and Pisani-Ferry, it took very little time for the authors of the Independent Annual Growth Survey (Timbeau et al. 2014) to evaluate the Juncker Plan critically and to call for a more robust and comprehensive approach. This group of progressive economists saw a chance to connect the investment agenda with an ambitious industrial policy, and in particular to contribute in this way to the Green Transition.

Thanks to the Juncker Plan, the work of the EIB has received a lot more attention than before, and it also helped to develop a more positive general attitude towards "national promotional banks". On the other hand, to see to what extent the Plan contributed to European recovery and the reduction of the "investment gap" requires careful judgement. It is a matter of debate whether more risk-taking is really happening or not (in the absence of ECB backing of the EFSI instrument), or whether EFSI is crowding out other instruments. And even if the EU cushion can mobilise more finance, the EU capacity to influence project selection remains very limited (can the EUR 16 billion tail really wag the EUR 300 billion dog?). This leads to broader questions about whether the EU actually has an investment strategy underpinning the MFF and related instruments, and how consequential that strategy is.

Cautiously, we can conclude that continuing this initiative can sustain a positive impact in the future, especially with regard to the continuation of a general pro-investment and anti-austerity discourse. But expectations should not be inflated, especially concerning the capacity of Juncker Plan–type financing to replace other forms of EU support.

For the InvestEU programme,[42] included in the new MFF proposal, to make a qualitative difference, critiques of the Juncker Plan – both early and more recent ones – will have to be taken into account. It would be crucial to specify what forms of investment are needed in which parts of the EU, which is far from being a uniform economic space. The eurozone imbalances also need to be taken into account. In the North and in particular in countries with current account surpluses, there is a need and space for massive infrastructure investment. On the other hand, in the South, or in countries experiencing stagnation and fiscal challenges at the same time, the key question is how to boost investment in productive companies. The capacity of enterprises with growth potential to access the equity market is a key question. In the East, whether inside or outside the euro-zone, overcoming the middle-income trap has become a major issue, and a strategic investment plan should be able to help in this effort.

42 In the new MFF the InvestEU is aiming at EUR 650 billion in additional investment. Beyond private and public finance, together with guarantees, support would be provided through an advisory hub and an accessible database bringing together projects and investors.

4.7 CONDITIONALITY: ENDOGENOUS AND EXOGENOUS

Current debates about the purposes and functioning of these instruments revolve around the concept of conditionality,[43] which is supposed to be widened and strengthened. When speaking about eradicating abuses and strengthening the link between policies and budgets in this way, the focus shifts to Cohesion Policy (three EU funds amounting to over one-third of the budget). But conditionality has different meanings and different effects, depending on the different types: the so-called ex ante, the macroeconomic and the newly emerging political conditionalities.

Ex ante conditionality means that before a programme can be launched from the structural funds (now "ESIF"), specific measures have to be taken in order to ensure that spending money in a particular area leads to the expected result. The content of such conditionalities is usually developed in line with EU policy guidelines and country-specific recommendations (CSRs). The experience with such ex ante conditionalities is largely positive and helps ESIF funds demonstrate not only a net GDP growth effect but also a transformative impact (towards "smart, sustainable and inclusive growth").

Macroeconomic conditionality, on the other hand, means that the normal flow of EU funds can be interrupted and funds can be withdrawn if the country violates the Stability and Growth Pact (SGP). This rule has been part of the game ever since Maastricht for the Cohesion Fund, but in 2011 the Commission suddenly proposed it for all the ESIF funds. The European Parliament and the Committee of the Regions were not united in support. It has many problems, starting with the fact that it would punish regions (and the more disadvantaged ones at that) for the failures of the central government of a country. Macroeconomic conditionality kills one of the most important features of the structural funds, namely that they provide certainty and security of investment resources in low-income regions. One should note that in recent years the EU has managed to bring down excessive deficits, without the macroeconomic conditionality playing any significant role. It was introduced at a time when pro-cyclical fiscal policy was trendy, which it is not today. No harm would come from dropping it.

Instead of reconfirming the macroeconomic conditionality, the zeitgeist today points towards new, namely political conditionality. There are rogue states inside the EU, promoting an illiberal counter-revolution. Hungary and then Poland have introduced problematic constitutional changes weakening the rule of law, and have whipped up opposition to the burden-sharing policies the EU rolled out in 2015 to tackle the immigration emergency. Should they continue to receive EU funds as before? Well, things have to change, but we need

43 A comprehensive overview of EU spending and conditionality is provided by Viţă (2017).

to think first about what exactly needs to be done and what would be counter-productive.

With the new MFF proposal, the Commission is proposing a new mechanism[44] to protect the EU budget from financial risks linked to generalised deficiencies regarding the rule of law in some member states. Regarding political conditionality, again the question arises of whether poorer regions should suffer because of recalcitrant governments. The instrument to be invented must allow even-handed intervention, which is not necessarily the case here, given the risk of illiberal populists coming to power even in higher income countries such as the Netherlands, France or Italy, which are not so dependent on investment support from the EU budget. If the defence of the rule of law becomes an EU policy, it requires instruments that can be used in all member states with equal effect. Sanctions without a proper focus and without guarantees against double standards may backfire politically and strengthen the hand of nationalist forces at all levels.

Conditionality can result in better functioning, but the right types and doses have to be found. For that purpose one should distinguish between endogenous and exogenous conditionalities. The first category (involving ex ante conditionalities) restricts the choices of the beneficiaries and helps to ensure that the instrument delivers on its mandate. The second widens the scope of objectives, and thus dilutes the original mandate of the instrument, potentially leading to weaker performance with regard to the original goals (in this case: economic, social and territorial cohesion). Such exogenous conditionalities, whether they concern fiscal austerity or structural reforms, have to be handled with care, and confusion of the goals of cohesion and convergence should be avoided if possible. In a policy area that is primarily about support, enabling rather than disciplinary innovations would be more consistent.

4.8 ABUSE OF FUNDS AND THE RULE OF LAW

When presenting the new MFF proposal on 2 May 2018, Jean-Claude Juncker was quoted as saying that “We will ensure sound financial management through the first ever rule of law mechanism. This is what it means to act responsibly with our taxpayers' money.” Without doubting the good intention behind these words, one should notice the confusion it creates. Tackling problems with the rule of law and the quality of democracy is indeed important, but the EU’s capacity to stamp out abuses of EU funds has to be strengthened also in countries that do not give rise to serious concerns about the rule of law. For a start, it has to be recognised that we are speaking about two problems and not one.

Concerning the rule of law, the issue is that after a country becomes a member of the EU, there is no way to enforce the Copenhagen criteria,[45] except under Article 7 of the Treaty,[46] which has proven very hard to use. In response to one major and several smaller cases raising rule of law-related concerns, the Commission designed a new mechanism for enforcement, which has been tested vis-à-vis Poland. Overall the past decade has shown that while the EU has successfully enforced the Maastricht criteria, it has failed to do so with regard to the Copenhagen criteria; apparently the EU considers the first more important than the second.

Being stuck with a rule-of-law problem does not mean that there would be no progress in the fight against fraud and abuse. In recent years, steps have been taken towards establishing an EU prosecutor with power to pursue judicial remedies if EU funds are abused. Such an EU prosecutor with powers beyond OLAF is a good idea, but such action is possible ex post, that is, after misuse has already happened. In recent years, however, new practices have also been developed to prevent abuses, and thought could be given to building on them. It is probably fair to say that the EU has been fairly successful in tackling abuses, other than systemic ones. Hence the link between abuses and the rule of law.

The Commission can already interrupt payments and suspend programmes if there is a strong suspicion of abuse, and less than 100 per cent confidence in the integrity of management or auditing at the national level. Such interruptions and suspensions can lead to financial corrections and delays but, under the current framework, the member state does not lose the relevant resources or control over the funds. One possible incentive for better performance would be to transfer funds that suffer major delays due to interruptions and suspensions into direct management by the Commission. The bulk of funds would still remain in shared (member state) management, but the country in question would be incentivised to avoid losing control and to correct behaviour. The Commission would need to invest in management capacity, but the returns on that investment would be significant in both financial and ethical terms. This solution would be far superior to linking the disbursement to “rule of law” conditionality, not least because it can take what seems like eternity to establish that this or that country is actually violating the values and democratic standards of the EU.

There is no better example than Hungary in this respect, where many pro-Europeans have the feeling that the EU has actually rewarded a rogue leader instead of punishing him (see Győrfi et al. 2016). When Viktor Orbán was re-elected prime minister, he started to create something similar to what was known as “the family” (semya) under Russian leader Boris Yeltsin twenty years before. The transfer of assets and grants

44 The proposed tools would allow the Union to suspend, reduce or restrict access to EU funding in a manner proportionate to the nature, gravity and scope of the rule-of-law deficiencies. Such a decision would be proposed by the Commission and adopted by the Council through reverse qualified majority voting.

45 The Copenhagen criteria, as defined by the European Council (1993), are the essential conditions all candidate countries must satisfy to become a member state. These are: (1) political criteria: stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities; (2) economic criteria: a functioning market economy and the capacity to cope with competition and market forces; and (3) administrative and institutional capacity to effectively implement the acquis and ability to take on the obligations of membership.

46 Article 7 is an EU infringement procedure to be used against member countries that have committed fundamental rights violations. It has two parts. Article 7.1 would allow the Council to issue a formal warning to any country accused of violating fundamental rights. If that doesn’t have the desired effect, Article 7.2 would impose sanctions and suspend voting rights. The first version of this appeared with the Treaty of Amsterdam (1999), after negotiations about eastward EU enlargement were launched.

(including EU funds) in large quantities to those close to the leader is certainly not in keeping with the intended mission of EU Cohesion Policy. Notwithstanding this woeful waste of resources, Orbán's political "family" (the European People's Party (EPP)) has been defending him from the consequences of his rogue behaviour, perhaps to avoid the stigma and the loss of a dozen EP seats. It is of course for the EPP to decide about its domestic affairs, but without enforcing different practices EU Cohesion Policy will continue to lose support as well as resources, leading not only to moral but also economic disintegration.

If the Commission had the power to take part of structural fund allocations for "a problematic country" under its direct management, still for the benefit of the country's development but bypassing the rogue government's corrupt network, better results could be achieved both in developing the country and in enforcing the rule of law. A precedent that shows that a management shift can be implemented comes from Greece where, at the time of the crisis, a Task Force was established to assist reforms and also the implementation of EU funds. At a time of arduous national effort, this form of EU support was appreciated.

4.9 INTEGRITY AND REFORMED MANAGEMENT

Abuse of EU funds means that common resources are diverted from the needs they are meant to serve. One way this can happen is to adjust the timing of disbursement to the political cycle in a particular member state. While seemingly an innocent trick, this can result in rushed pre-election project dumping to the detriment of project quality and lack of sufficient funds in the following governmental period. The way to deal with such political cycles is to introduce a reasonable annual ceiling that cannot be exceeded within the national context.

While the ESIF (supporting regional and social development) is proverbially complicated and requires a large amount of paperwork, a large part of the excess burden actually comes from the member states, and it can be extremely difficult to control after the fact whether public and private actors always strive towards best practices and do not try to game the system. For example, Dellmuth and Schraff (2017) observe that the "implementation of European Structural and Investment Funds faces serious challenges. Electoral institutions play a central role in determining the degree of vote-buying. Domestic politicians pursue their own electoral interests with EU funding, whereby vote-buying is more pronounced under majority voting than under proportional representation. This distorts a needs-based allocation of the ESIF." Their findings suggest that "vote-buying with EU funds is more common under majority voting than under proportional representation".

Complications are often linked to too many levels of management, which can be addressed by creating new organisational structures within the member states, or shifting the boundary between direct and indirect management of structural funds. One can also consider a third way between direct and shared management, namely assisted management. This operational form would not call into question the legitimacy and dominance of shared management in Cohesion Policy, but it would provide direct assistance with manifest weaknesses of audit management in the relevant member state. For example, just as national experts can be assigned to various directorates of the Commission to reinforce EU staff, EU staff could be posted to member states in order to boost the capacity of managing authorities as well as of beneficiaries. For this purpose, Fabrizio Barca (2017) recommends hiring 300 young professionals who can help with administrative work at the local level, especially in disadvantaged regions. This sounds like a large number for a staff surge, but it would also allow for savings elsewhere and such a move would visibly improve the effectiveness of EU funds, protect sound financial management and demonstrate EU assistance in regions and localities where it is needed most.

Some of the controversies of recent years can be tackled by investing in administrative capacity (in the member state), but such spending categories must have their reasonable limit. The point is that, with Eastward enlargement, the EU extended a funding method that had performed reasonably well in advanced economies to a region that had barely passed the transition stage to the market system and was not fully prepared to handle large transfers. The low absorption rates in Romania highlighted the great administrative difficulties in some Eastern states, and a couple of debacles in the Czech Republic[47] (now Czechia) have shown that not even in the most advanced "new member states" can smooth functioning be taken for granted.

To be fair, some of the "older" member states also keep producing problematic results and high error rates (notably the South of Italy and various Spanish regions). By investing in management with a focus on and direct representation in the less developed regions the Commission would greatly enhance the effectiveness of Cohesion Policy. In such regions and localities, assisted management could be tested in the form of pilot projects. Before piling on new layers of conditionalities, one should think about reforming management and control mechanisms and avoid throwing out the baby with the bathwater.

OPERATIONAL ADVICE AND PROPOSALS

- Improve evaluation methods with the involvement of genuine stakeholders.
- Try to simplify access and implementation without risking quality of impact.
- Introduce safeguards, such as reasonable annual spending ceilings, against political cycles.
- Maintain financial engineering solutions without exaggerating their potential.
- Boost the capacity for protecting the integrity of EU funds (including prosecutor and OLAF).
- Create forms of assisted management (in addition to direct and indirect channels).

47 In 2012 all funds to the Czech Republic were suspended due to the lack of confidence in the audit system. In 2017, a former finance minister, currently Prime Minister, came under criminal investigation in connection with an earlier fraud with EU funds by one of his family's companies.

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SUMMARY AND CONCLUSIONS

In 2018–2019, the European Union is designing its new long-term budget amidst a variety of external and internal challenges, some of which are certainly not temporary. Political attacks from inside and outside, together with multiple imbalances, require bold answers and it is doubtful that a consensual fiscal solution can be worked out under such strict time pressure.

Brexit, which is a high-risk event for both sides but especially the United Kingdom itself, is having a direct impact on the EU budget, with a variety of consequences. It should not be allowed to play a purely negative role in the process of EU reconstruction and EU budget planning, however. It is important to rebut false and hostile criticisms of the EU and to address the underlying causes of Brexit in policy as well as budgetary terms.

Lessons must be learned on both sides of the Channel, including in terms of political economy. There have been and always will be enemies of European integration, but they will appeal to wider audiences only if the EU fails to deliver economic growth and do so in an inclusive way. Therefore Brussels debates in the current situation have to focus more on how to create and share prosperity. The EU must find ways to invest more, including in its own better functioning.

For the EU the strong link between policies and funding is a source of credibility. Under the current pre-federal model, however, the EU coordinates policies instead of governing, and it is bound to leverage private and public funds in addition to spending its own modest resources. There are limits to this model, and its adequacy or resilience has to be assessed against increasing heterogeneity inside and Europe's diminishing share of the world economy outside. The EU may be at an historic turning point at which citizens and member states expect much more from it, while there is hesitation in several finance ministries about providing more resources.

Brexit and other lessons should lead to a stronger and not weaker EU role on related social and regional policies, instead of leaving them to the member states. Cities and NUTS 2 regions have to be empowered and allowed to have more direct linkages to the EU level, as part of a broader encouragement to pursue complex and robust development strategies.

Considering instruments old or new should not be the main driver of decisions on allocations. With the CAP the key question is not its overall size but the effects on income distribution and environmental protection. Improving income fairness in the CAP should be prioritised over budget reductions.

Cohesion is not a peripheral policy area; it belongs to the core mission of the European Union and therefore its funding has to continue at a level comparable to the recent past. The effectiveness of Cohesion Policy must improve, however, in particular through smart conditionality and innovation in the management system. Such changes are also needed to rebuild trust in the EU budget and its modest redistributive role.

Conditionality is an important principle, but it also has limits. Cohesion instruments can improve, but they cannot become overly tricky so as to combine delivering economic and social convergence, tackling business cycles, safeguarding fiscal discipline and sanctioning political degeneration as well. To avoid functional confusion, the EU needs to maintain a wider range of instruments, and generate innovative solutions in relation to fiscal capacity in the euro-zone and the management of Cohesion Policy instruments. In combination this requires more resources than in the past.

Political debates should go beyond the changing size of various envelopes. The recent crises call for serious reflection on the economics of the EU budget and, based on experience, some of the operational questions can be deemed as important as political or macroeconomic ones. Answering those, with openness to innovation, can help to bring various stakeholders on board for a more ambitious and more prosperous EU.

Ongoing discussions on fiscal policy and budgetary instruments play a pivotal role in the pursuit of a well-functioning EU and a more prosperous and balanced European economy. The stakes are high, and lessons have to be drawn from the recent crises. In the absence of orderly transfers accompanying fiscal discipline rules, the Monetary Union may collapse. And if the current budget debate leads to a significant reduction of transfers by downgrading the cohesion funding instruments, the single market may also disintegrate. The EU should not resolve one problem by creating or aggravating others.

Under time pressure, a low-ambition compromise might be possible between those net contributors who want to provide less and those net recipients who want to see fewer conditions. This, however, is the model of a weak EU, unprepared for the shocks and transformations of the future. The EU has emerged from the financial crisis but society's wounds have not been healed and tools to ensure economic resilience are still lacking.

If the EU were a company, it would now need a capital increase. It has to invest in a new business model, not least to preserve its social achievements and political values. This might also require a new model budget, some key elements of which we have outlined in this study.

POLITICAL, ECONOMIC AND OPERATIONAL ADVICE AND PROPOSALS

- Advocate an increase of the MFF ceilings in view of newly identified common needs and goals.
- Enhance genuine own resources for the EU budget (to replace part of national contributions).
- Support EU funding to boost security and productivity without calling into question core functions of the EU budget, such as cohesion and convergence.
- Pool resources for common defence and more harmonious living with our neighbourhood.
- Strengthen the social dimension of the MFF (in qualitative terms, beyond pooling existing instruments).
- Use the example of the MacDougall Report for an inquiry into a more robust EU budget.
- Maintain the MFF allocation functions (and invest in improving their delivery capacity).
- Double the funding of research and innovation to change the European business model.
- Establish a proper euro-zone stabilisation capacity, if possible with a focus on fluctuations of unemployment.

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- Introduce a modest levy on current account surpluses as another form of EU own resource.
- Enhance the EU's fiscal capacity to deal with globalisation effects and climate change.
- Improve evaluation methods with the involvement of genuine stakeholders.
- Try to simplify access and implementation without risking quality of impact.
- Introduce safeguards, such as reasonable annual spending ceilings, against political cycles.
- Maintain financial engineering solutions without exaggerating their potential.
- Boost the capacity to protect the integrity of EU funds (including prosecutor and OLAF).
- Create forms of assisted management (in addition to direct and indirect channels).

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List of Abbreviations

EU financial instruments

AMIF	Asylum, Migration and Integration Fund
CAP	Common Agricultural Policy
CCI	Competitiveness and Convergence Instrument
CEF	Connecting Europe Facility
CF	Cohesion Fund
EAFRD	European Agricultural Fund for Rural Development
EaSI	EU programme for Employment and Social Innovation
EDF	European Defence Fund
EDF	European Development Fund
EFSI	European Fund for Strategic Investment
EGF	European Globalisation Adjustment Fund
EISF	European Investment Stabilisation Function
EMFF	European Maritime and Fisheries Fund
ERDF	European Regional Development Fund
ESF (ESF+)	European Social Fund
ESIF	European Structural and Investment Funds
EUSF	EU Solidarity Fund
FEAD	Fund for European Aid to the Most Deprived
MFF	Multiannual Financial Framework
RSP	Reform Support Programme
YEI	Youth Employment Initiative

Other abbreviations

CCCTB	Common Consolidated Corporate Tax Base
CPR	Common Provision Regulation
CSRs	Country Specific Recommendations
EBRD	European Bank for Reconstruction and Development
ECA	European Court of Auditors
EIB	European Investment Bank
EMU	Economic and Monetary Union
EP	European Parliament
EPP	European People's Party
EPSR	European Pillar of Social Rights
FTT	Financial Transaction Tax
GDP	Gross Domestic Product
GNI	Gross National Income
ILO	International Labour Organization
IMF	International Monetary Fund
MEPs	Members of the European Parliament
MIP	Macroeconomic Imbalances Procedure
NUTS	Nomenclature d'unités territoriales statistiques (FR)
OECD	Organisation for Economic Co-operation and Development
OLAF	Office européen de lutte antifraude (FR)
PES	Party of European Socialists
SDGs	Sustainable Development Goals
TFEU	Treaty on the Functioning of the European Union
UNFCCC	United Nations Framework Convention on Climate Change

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