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The EU Budget Review - Does Britain need its rebate?

20 March 2009

Conference Report

On the 20th of March 2009 The Federal Trust held a conference entitled, 'The EU Budget Review – Does Britain Need its Rebate?' **Brendan Donnelly** opened the conference as convenor and Director of the Federal Trust, and chaired the meeting. He began proceedings by thanking the Commission Representation in the UK for making this event possible and then went on to introduce the first speaker, **Stefan Lehner** - Research Head of Unit: Directorate-General on Budgetary and Financial Affairs at the European Commission.

Mr. Lehner's presentation focused upon how to reform the EU budget in line with changing global priorities, a topic that has been at the centre of his research since the Commission gave him this mandate in 2006 to undertake a far reaching budget review. The Commission has made budgetary reform a priority of the highest degree, knowing that how the budget is structured will ultimately define the delivery of EU policy. The Commission recognizes that the substance of the budget must be changed in order to 'build a new consensus' and to realign the future priorities of the EU budget with the priorities of its members.

Against this background, the Commission undertook in 2007 and 2008 a 'consultation exercise,' which was completed on the 15th of June 2008 attracting over 300 contributions from a wide spectrum of organisations including universities, NGOs and representative groups from the regional level all over Europe. This consultation brought to the attention of Mr Lehner issues that were considered to be (or at least should be) the top priorities to be addressed in the EU budget. These were climate change and energy, especially guaranteeing energy supply security (the need for which became only too apparent in January with the dispute between Russia and the Ukraine). In addition to these topics other areas of concern were repeatedly mentioned, including the reduction of inequality between countries, threatening demographic trends (especially Europe's shrinking population) and also co-ordinating a response to external security threats against the Union.

Mr. Lehner and his colleagues are concentrating their attention on two principal issues:

What form will this new direction for EU spending take?
Can we promote cohesion by changing the instruments of budgetary action?

Mr. Lehner told us that his work has been made significantly harder by 'unforeseen developments.' The fluctuating oil price has led to pessimistic economic expectations in the long term. The 'no-vote' returned from the Irish referendum has meant a lack of clarity complicating the outlook of the future EU task. Climate change is fast becoming one of civilisation's most pressing issues and the EU must adapt to this by affirming it as a priority and reallocating the budget to reflect this, especially as 'recent indicators are providing the worse than worse case scenarios.' Above all the financial crisis and looming recession remain pressing, but Mr Lehner suggested there is an opportunity to treat this period as a catalyst for enacting change and foresees a strengthened

This conference was financially supported by the European Commission Representation UK

EU budget that could take a leading role in supporting EU economies in an attempt to put a stop to cyclical economic patterns. The Commission will make detailed proposals by spring 2011.

The next speaker was former advisor on European matters to Tony Blair and Vice-Chair at the Policy Network, **Mr Roger Liddle**, who came to provide us with a talk entitled, 'a London view, not <u>the</u> London view,' examining the relationship between the UK and the EU budget. He came into Downing Street in 1997, and upon his entry was told that he had to maintain two British policies. First, that the UK abatement remained totally 'non-negotiable,' and secondly to keep the EU budget as low as possible so that the UK would contribute only the bare minimum. In order to achieve this aim in particular there was a degree of political positioning between member states, whereby the UK would ally itself with those considered to be 'budget disciplinarians' and net contributors, such as the Dutch, the Swedes and the Germans. This desire for budget discipline was echoed at the Treasury, according to Mr Liddle, as in 1997 the Treasury's view was that certain EU policies didn't provide good 'value for money' and as such certain British departments were adverse to commit to European spending initiatives, in particular structural funds, which required matched funding in the form of national public-spending. But despite this hostility Mr Liddle gave examples of the 'intellectual agility' Britain showed while pressing for objective 1 funding, such as the reclassification of regional boundaries and arguing special cases for our 'highlands and islands.' A further example of Britain's simultaneous desire to keep its own contributions down, but simultaneously employ creative methods to gain the most resources from existing European policies could be seen in British attitudes toward the Common Agricultural Policy (CAP) in 1997. At that stage British officials and politicians had not understood, as they later came to understand, that substantial reform on the issue of CAP could only be achieved by a 'history making decision' by European leaders, taking perhaps the form of a 'trade-off,' whereby Britain would relinquish its rebate if France were to reduce the number of its farmers reliant upon CAP subsidies. In 1997 British policy remained totally resistant to such a trade-off, but with time Mr. Blair came to understand the desirability of such a "grand bargain." Unfortunately, by the time of the British Presidency of the European Union in 2005, when such an overarching budgetary settlement might have been possible, the general political background had become more complicated.

The British government has always been an enthusiastic supporter of the enlargement of the Union. Its approach, however, to the budgetary consequences of this enlargement did not always gain the sympathy of either the new or existing members of the Union. New members viewed with suspicion the British argument that direct payments to them from the Union's budget should be phased in over time, as their national administrations become better able to make effective use of these new resources. Existing members firmly rejected the British suggestion that in future transfers between richer and poorer members of the Union, notably the Central and Eastern European countries, should primarily take place on a netted-out cash basis. The German government has always been especially vocal in its insistence that there must continue to be specific European projects, demonstrably funded by the Union, carried out in Germany, above all in the former East Germany.

All these issues came to a head in the budgetary negotiations of 2005. The objective consequence of enlargement was, in the short term, to make more difficult any radical reform of the European budget, as both new and longer-established members of the Union sought to defend their legitimate interests and their anticipated advantages. Significantly from the British point of view, the Council agreed in 2005 on a different method of calculating the British rebate/abatement, whereby the arrangement would no longer apply to "those elements of Community expenditure which related to new member states." This was in response to an effective campaign mounted by the new member states in protest at what they saw as their contribution to the British rebate/abatement, a campaign which embarrassed the British government and gained predictable sympathy from those of Britain's partners who themselves are far from enthusiastic contributors to the British rebate/abatement. The change in the method of calculating the British rebate/abatement led to further consequential and complicating amendments to the budgetary contributions of a number of other member states. The current structure of the European budget is far more complicated than the original outline drawn up at Fontainebleau in 1984.

The budgetary review set up by the European Council of 2005 will have in Mr. Liddle's view, its work cut out. The limited success of British negotiating tactics in the period leading up to the agreement in 2005 is a warning to all governments of the need to consider a wide range of perceived national interests in the development of negotiating tactics likely to be successful and persuasive. Three main challenges face the review.

The first is the continuing reform of the Common Agricultural Policy. One realistic area for change would be for the substantial reform of the cereal sector. This is an important part of the CAP but sufficiently specific and limited an area of reform to be potentially achievable. The second urgent issue is that there remains inadequate funding for a number of expenditures that are undoubtedly best implemented at the European level. Worth particular mention in this context are research and development, the European Neighbourhood Policy, the protection of the Union's common external borders and, above all, climate change. The recognition of these European priorities needs to be reinforced with a new emphasis placed upon them in the formation of future EU budgets. Finally, a greater linkage would be desirable between the Union's budget and current EU economic and social reform programmes. The current financial crisis has made the argument for this linkage more compelling than ever before.

The final speaker at the conference was **Dr. Robert Ackrill**, a Lecturer at Nottingham Business School, Nottingham Trent University, who spoke on the topic of, 'Is a rational EU budget possible?.' In order to assess the budget's status as rational (or not) Dr. Ackrill began by addressing its composition, in particular its revenue and own resources, suggesting these are important as they provide a degree of independence for the EU. He provided an overview of the different methods of contributions including Gross National Income (GNI), and VAT own-resource contributions, remarking on how VAT-based contributions peaked in 1968 and that there is now a marked preference toward GNI contributions, which account for 3/5th's of total EU revenue. Despite this change in the methods of raising the Union's budgetary resources, expenditure choices for the Union and its member states had remained remarkably constant.

Dr. Ackrill's next point of interest referred to EU spending choices in relation to member states. With regard to macroeconomic stabilisation, he asserted that this will not have a role in the future EU budget, with macroeconomic instruments being retained at the national level. Turning to the redistributive and allocational tasks of the European and national budgets, he noted how different members of the EU approach this function, with some states far more interventionist whereas others opt for markedly less fiscal activity in these fields. He reinforced this opinion with detailed and informative graphs proving a strong correlation between national GDP and the member state's contribution to the European Union's revenues, but a far weaker correlation in relation to expenditure. Dr. Ackrill then offered some general observations, especially in relation to net balances of the budget, and how distributional reform has been blocked by member states capping EU spending, thereby creating a 'zero-sum or even negative game.' Despite the fact some things change, said Ackrill, revenues, payments, and distribution of transfers have remained within the European budget remarkably stable over many years. In response to the questions following this presentation Dr. Ackrill concluded that there are clear 'rationales for it [the EU budget]' with revenues and decision-making policy preferences set and distinguishable to outside analysts. There remains in his view no clear evidence that there will be in the European budget significant change for the foreseeable future, whether generated internally or by external circumstances. Such reform as there is will be 'glacially slow.'