



## The Future EU Budget

-What changes, what stays and the implications for Romania-

Author: Mihai Panaite

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## CONTENTS

<b>INTRODUCTION</b> .....	3
<b>NOTES ON SEVERAL ASPECTS OF THE EC PROPOSAL</b> .....	3
WHO WILL APPROVE THE BUDGET AND HOW WILL THIS WORK? .....	4
NEW REVENUES FOR THE EU? .....	5
<b>WHERE DOES ROMANIA STAND?</b> .....	7
<b>WHAT WILL HAPPEN NEXT?</b> .....	7

## INTRODUCTION

*CRPE issued the “Romania and the EU budget reform” report in March 2010, bringing up, among other topics, the possible structure of the future multiannual financial framework (MFF). We now have a specific proposal: at the end of June 2011, the Commission launched its proposal for the next MFF (2014 - 2020). This policy brief sets out to present the main novelties and to point out Romania’s weaknesses in the context of the forthcoming negotiations.*

This will be the fifth MFF, and the first MFF adopted according to the new EU Treaty provisions. Also, it follows the 2009 public consultation on the future European budget. Given the unanimity rule of the Council, the Commission’s proposal is ambitious, but not revolutionary (an evolution rather than a revolution). We anticipated this in last year’s report<sup>1</sup>.

The most important novelty lies in the way the European budget will be financed, namely the proposal to adopt a new resource – a tax on financial transactions. This is an older desire of some Member States: they proposed the establishment of such a tax at international level and promoted the idea in the G20 framework, but to no avail.

## NOTES ON SEVERAL ASPECTS OF THE EC PROPOSAL

A mere glance at the new expenditure categories<sup>2</sup> confirms our last years’ prediction regarding a priority switch from agriculture to research and innovation. However, the magnitude of this change is moderate. Basically, the allocations for agriculture will freeze in 2013, which means a reduction of their share from the total MMF, while research expenses will increase significantly (however, they start from a modest amount).

The cohesion policy will benefit from slightly increased allocations and will comprise a new instrument, the Connecting Europe Facility. Another novelty was brought by the proposal to set up a 5% reserve from each Member State’s quota, which could only be used by those states with the best performance in managing funds.

**The Connecting Europe Facility should help accelerate the large transport, energy and communications infrastructure projects.**

<sup>1</sup> CRPE, Romania and the reform of the EU budget, Policy Memo nr. 8, București, Martie 2010, [http://www.crpe.ro/library/files/crpe\\_policy\\_memo\\_8\\_ro.pdf](http://www.crpe.ro/library/files/crpe_policy_memo_8_ro.pdf)

<sup>2</sup> European Commission – Multiannual Financial Framework: Questions and answers, Memo/11/468, Bruxelles, 29 iunie 2011.

The Commission's proposal also concerns some technical aspects of the multiannual financial framework. The optimal duration of a MFF is still put into question. All MFFs, except for the first one, were planned for 7 years, but the Lisbon Treaty creates the premises for a review, by establishing a minimum duration of 5 years. There are voices suggesting that the MFF should be reduced to 5 years and connected to the European political cycle (both European Parliament and Commission have 5 years mandates). However, the Commission's proposal is structured on seven years, in order to streamline the adoption process.

**Which is the most appropriate timeframe for a MFF?**

The current five categories structure (competitiveness, agriculture, citizenship, foreign affairs and administration) allows for minimal flexibility, as the possibilities to reallocate money between categories are limited. The limits for each category can only be exceeded under specific circumstances, and not significantly. Thus, a structure with fewer categories would provide a greater flexibility. The European Parliament's budget proposal comprises only three categories: Europe 2020 (including all actions for achieving its goals), Global Europe (including external actions) and Administration<sup>3</sup>.

*Such a classification has the advantage of financially highlighting the Europe 2020 Strategy, which is the EU's main strategic plan and must be provided adequate funding in order to achieve its goals.*

### **Who will approve the budget and how will this work?**

Under the EU Treaty (Article 312), the MFF has to be unanimously approved by the Council and has to get the Parliament's approval by a majority vote – the so-called consent procedure. This procedure implies that the actual negotiations on the future MFF will be carried out between the Member States. The Parliament can only accept or reject the financial framework, it cannot submit any amendments. Virtually, the driver's seat is occupied by the Council, while the Parliament has only a formal role, approving Member States' decisions.

However, the political practice following the Lisbon Treaty will modify this institutional arrangement. The EU legislative is not satisfied with only a yes or no option, it wants to be entitled to make amendments.

One year ago, the Parliament established a Special Commission on political challenges and budgetary resources for a sustainable post-2013 European Union. Also, shortly before the presentation of the

**The Parliament is unhappy with its role and displays budgetary activism.**

<sup>3</sup> Non-legislative resolution: „Investing in the future of Europe: a new Multiannual Financial Framework for a competitive, sustainable and inclusive Europe”, INI/2010/2211, European Parliament.

Commission proposal for the 2014-2020 MMF, it adopted its own vision of the future budget, shaped as a resolution (INI/2010/2211).

In this document the Parliament “reminds” that the adoption of a new MFF cannot be done without its consent and requires the rapid establishment of a work procedure which would include the Parliament, Council and Commission. As mentioned above, what European Parliament really aims to is to get involved in designing the new financial framework, instead of simply approving (or not) the Member States’ decisions.

The Parliament knows that its advantage, the power to reject the new MFF, is not such a fearsome political weapon as it might seem, because using it would have a negative impact on everyone involved (including itself). What if it actually rejects the proposed budget? The budget limits from the last year of the preceding MFF are applied. Although it might threaten with a negative vote, the Parliament aims at increasing the EU budget; therefore it will avoid extending the 2013 provisions.

The Parliament’s involvement will not necessarily complicate the situation. Two opposing groups will inevitably appear within the Council: the first one will include the net contributors who will ask for a limited European budget, while the second will comprise of new Member States and the Parliament which will request a larger budget. In fact, the first signals in this direction have already appeared. From this perspective, we suspect that the group in favor of a larger budget has already emerged, opposing the contributors’ group.

**In December 2010, a group of five Member States (UK, Germany, France, Netherlands and Finland) asked the President of the Commission to propose a frozen budget for 2013.**

*However, considering the Council’s unanimity rule and the Parliament’s consent requirement one can expect the new multiannual financial framework to be a compromise - acceptable for all involved.*

### **New revenues for the EU?**

With regard to EU’s own resources system, things are slightly different. There is a specific procedure concerning the introduction of taxation on financial transactions: the Council takes all decisions (by consensus), while the Parliament is only involved through the consultation procedure (Article 311 of the Treaty).

**A tax on financial transactions is not easy to introduce because of its potential implications.**

This means that, no matter the Parliament’s opinion, the Council is free to take its own decisions. In addition, the decision on modifying EU’s own resources system, if such a decision was taken,

would not pass unless each Member State approved it according to its own constitutional procedure.

Currently, the European revenues consist of:

- traditional own resources (mainly custom duties, approx. 14% of the total);
- VAT – based resource (approx. 11% of the total);
- miscellaneous revenues (approx. 1% of the total consisting of revenues from fines and taxes applied to EU officials’ salaries);
- Member States’ contributions, the so-called revenue based on the gross national income (GNI); the rest up to 100%.

The last year’s CRPE assumptions are partially confirmed by the fact that the proposal for a new EU own resources system includes significant changes. Thus, the current VAT-based resource would disappear, being replaced by an upgraded one. This would involve a simplified and transparent process by which a share of the VAT collected by Member States is transmitted to Brussels. However, the extent to which the collected

**The modernized VAT resource would require the transfer to the European budget of maximum 2% from the VAT for goods and services collected in each Member State.**

amounts would be affected by the differences between countries (in terms of consumption and standard rates) is unclear. It remains to be seen once the final document is published.

A second important proposal, which we have not foreseen in the 2010 report, concerns the establishment of an own resource based on a tax on financial transactions. This would be applied to financial institutions – in the widest sense of the word –, including banks, investment funds, insurance companies, etc. An actual rate would be determined later. The two new resources could provide up to 40% of the EU budget for 2020, while the GNI-based contributions would automatically decrease. Since this means a decrease in direct money transfers from Member States to the EU, the Commission hopes for their consent on reforming the system.

Considering that the potential contributors - financial institutions- are gathered in a few major financial centers (London is by far the most significant), it is obvious that the money will come from the countries where these centers are located. An additional tax could cause financial centers to lose competitiveness, leading to a potential relocation of activities and a loss of revenue from taxes in the affected states, together with a decreased status and influence.

Decision makers in Brussels should consider the Swedish example: in the 80’s Sweden introduced a tax on financial transactions which led to transactions’ migration to other financial centers. The tax was abandoned in the early 90’s because the collected amounts were far below expectations<sup>4</sup>.

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<sup>4</sup> Marion G. Wrobel - Taxes on financial transactions: the international experience and lessons for Canada, 1996

*Therefore, the establishment of a tax on financial transactions at EU level in the absence of an international agreement is problematic. The EU could lose market share in the field of financial services.*

A possible course of action could be that of charging a very low rate at first and renegotiating later within the G20, based on the first results. This has also been suggested by the president of the Commission<sup>5</sup>. As far as the Council negotiations are concerned, the first reactions show the support of several Member States and the British opposition. Although this tax would mainly affect UK, experience shows that solutions can be found in such cases when a Member State is affected in a disproportionate manner by the financial flows to and from the EU.

## WHERE DOES ROMANIA STAND?

Considering the disparities in terms of GDP per capita which Romania has to recover against developed countries in the EU, along with the increase of allocations for programs in agriculture by 2016, our country should obtain a favorable financial package.

**The Romanian representatives will go to negotiations without two major arguments: that money was spent and it was spent properly.**

However, the Romanian officials will go to negotiations without two major arguments: that money was spent and it was spent properly. This has two main reasons: first, the absorption of funds in the current MFF does not exceed, by any calculation, 5% of the total, and, second, some payments were frozen because of irregularities and some Member States' conviction that Romania is not a state of law.

Our country is expected to obtain not less than an acceptable financial package, since its interests and issues are similar with those of other countries (such as Poland) from the group asking for an increased European budget.

## WHAT WILL HAPPEN NEXT?

The proposal for a new MFF includes drafts of legislative acts to be adopted in this respect.

*The Commission estimates that the actual legislative proposals will be presented by the end of this year<sup>6</sup>. The negotiations could take place during the Danish and Cypriot presidency and the final agreement is expected to be achieved by the end of 2012.*

**The main legislative proposals:**

- **Regulation proposal for the new MFF**
- **Draft decision on the own resources system**
- **Proposal for a new inter-institutional agreement**

<sup>5</sup> Andrew Willis - Brussels seeks financial tax in new EU budget, EU Observer, June 20, 2011.

<sup>6</sup> Silvano Presa – The EU Budget and the Multiannual Financial Framework, Brussels, June 28, 2011

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## About the author:

**Mihai Panaite** is a CRPE affiliated expert. He worked as parliamentary assistant at the European Parliament, as economist at the Ministry of Finances (2002-2007) and he graduated the “European Political Economy” master program at London School of Economics.

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Translated by: Ioana Ivanov

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Romanian Center for European Policies (CRPE)

Știrbei Vodă 29

ap. 4, București - 1

[office@crpe.ro](mailto:office@crpe.ro)

Tel +4 0371.083.577

Fax. +4 0372.875.089

For further details about CRPE, please visit our website: [www.crpe.ro](http://www.crpe.ro)