

## Squaring the MFF circle: How match funding can deliver the EU's new priorities

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The informal EU summit has ended without a breakthrough on the size and details of the next Multiannual Financial Framework (MFF), the Union's multi-year budget from 2021 onwards. This is hardly surprising. We are only at the beginning of a long negotiation process that has always been contentious; more so this time due to the dual pressure of lower contributions - with the exit of the UK, one of the main net payers - and the need to finance the EU's pressing priorities - migration, internal and external security and possibly new instruments to strengthen the Economic and Monetary Union (EMU) as well as the accession process to the common currency.

### *Old and new conflicts*

Once again, there are significant differences between net payers who, at most, seem to be willing to close the gap left behind by the UK's departure but not to further increase the EU budget; and net recipients who fear that any cost cutting will be at their expense, in particular through reductions in cohesion funding and agriculture, the two main redistributive expenditure blocs.

In the background, there is a sweltering conflict on the use of 'conditionalities', whereby payments become contingent on the (mis)behaviour of member states. Some advocate a new democratic conditionality (to enforce respect for EU values and EU law) adding to the already existing macroeconomic conditionality (to enforce budgetary discipline). In part, this is driven by the feeling that some governments in Central and Eastern Europe showed a lack of solidarity in the migration crisis, explaining why an even more explicit link to migration quotas has also been in the debate. However, while many believe that the budget should create incentives for common actions, there are serious doubts over the long-term political effects of 'punishing' certain countries.

### *An impossible task?*

While the complexity of squaring the MFF circle has increased substantially, the negotiation process remains unchanged. At the end of the day it requires the unanimous consent of all 27 member states, in addition to the support of the European Parliament. This is a high hurdle to jump and creates a strong bias in favour of the *status quo*: politically it is often much easier not to deviate too far from existing provisions than to do something radically new. This is not to say that the budget has not changed over time: agriculture expenditures have gradually decreased while new priorities like research and innovation have found their way into the budget. This reprioritisation is set to continue: there already seems to be a strong consensus that research funding should, at the very least, be safeguarded in the current negotiations, despite the significant pressures on spending.

But this time around, incremental change will not be enough to deal with the dual pressure of Brexit and new priorities. If net payers are unwilling to go further, one way of closing the funding gap might be through the introduction of genuine 'own resource' for the EU, in the form of, for example, a carbon tax or a tax on digital or financial transactions. However, resistance among member states is high, which makes this scenario unlikely. So, if contributions are not further increased, there must be very significant cuts in agriculture and cohesion to balance the books. This would require a number of deep and comprehensive reforms to make these policies function with a lot less money but such an approach seems unlikely: in the end, a 'haircut' approach is a lot less effective but politically easier to sell.

### ***Deepening divisions?***

Politically, significant cuts in these policy areas would deepen the East/West divide. Downsizing the budget allocations for agriculture and cohesion would mostly affect the poorest countries; especially those with a greater primary sector in their economy. The sense of unfairness would be further exacerbated by the fact that these countries also (proportionately) benefit less from research funding.

For Southern Europe, many of the same concerns apply. However, for them the blow could be softened by new instruments (potentially outside the EU budgetary framework) that might channel investment and support to the weaker economies of the Eurozone. The reduction in economic importance of agriculture in Western European countries – that have been recipients of significant agricultural funding (namely France) in the past – has greatly reduced their financial interest in this policy area. Parts of cohesion spending, on the other hand, are often criticised as being ‘circular’ by richer countries, who see their financial contributions channelled through the Commission back into their regions.

### ***Squaring the circle***

So, how can we square the circle of budgetary pressures and competing priorities, while achieving a meaningful reform of the MFF and avoiding political conflict and fragmentation? There is no simple answer. As usual, it will require a great deal of political compromise but there is also a need for innovative approaches. There will certainly be a stronger emphasis on Financial Instruments, including the European Fund for Strategic Investments (EFSI), in order to shift EU spending from grants to loan-based instruments as these mechanisms offer the possibility to leverage private money. Spending areas such as a Eurozone budget might also be taken outside the EU budgetary framework, relieving some of the budgetary pressure but raising questions of governance, inclusiveness and oversight. But none of this budget engineering will ensure that the MFF delivers effectively on the current challenges the EU faces.

### ***Match funding***

An alternative route to explore is to use an adapted form of match funding already implemented in regional policy. For certain policy areas, funding could be made conditional on a combination of a demonstrated need and national financial contributions, matching the funding available from the EU. For example, this mechanism could be applied in the area of migration: those states that could evidence pressures on public services as a result of migration flows could apply for EU funding to match their (strained) funding of these public services. This could be organised in a funding pool, where EU funds would be pre-allocated by country according to needs. Untapped funds (i.e. not matched) could be reallocated to those countries that use the mechanism.

There are two advantages to such a financial mechanism: first, it is needs based; second, it is flexible in the sense that it would let member states decide whether they ‘buy into’ this policy area. Those member states arguing that this is ‘circular funding’ could simply opt out. As a result, the contribution of net payers would still be capped by the agreed ceiling of the EU budget, but the EU’s capacity to reach its objectives would be enhanced by leveraging member state spending. This could be a way of dealing with those (new) priorities that are not directly linked to cohesion or convergence objectives. This also ensures that there are incentives for those countries that commit to participating in delivering EU-wide objectives but without ‘punishing’ those countries that remain outside.

Such a mechanism still requires detailed work, especially as it would be politically contentious. But at this stage in the negotiations, we should keep an open mind, explore alternatives, and be ready even to experiment with new options. If not, we will, at best, get a fundamentally unreformed and geographically unbalanced budget, or at worst no agreement at all.

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