Reaction to Iozzo, Micossi and Salvemini, *A New Budget for the European Union?**

IAIN BEGG

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Iain Begg is a Professorial Research Fellow at the European Institute, London School of Economics and Political Science

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While it is true that the *juste retour* mentality that has increasingly pervaded budget negotiations since the last major reform twenty years ago has many regrettable characteristics, it will never be easy to arrive at a package of EU spending that escapes this particular curse. The Iozzo, Micossi and Salvemini paper is, therefore, a welcome attempt to find a new approach. It is one of a number of recent contributions to the budget debate that has sought to distinguish more explicitly between the public good and distributive elements of the budget.

In essence the proposal boils down to saying that the budget should be split, with public goods funded by authentic EU resources, while net transfers between Member States are financed by GNI-based contributions. It sounds alluring, but would have to confront a number of difficulties. Conceptually, to begin with, the first 'chapter' of spending in the proposal is a form of equalisation in which the transfers are embedded in selected policies, rather than being pure cash transfers as found in some federal countries. Good examples of the latter are the *finanzausgleich* mechanisms in Austria and Germany. Pure cash transfers have the advantage that they leave decisions on the use of the resources to the recipient, whereas using CAP or cohesion policy to effect net transfers imposes evident restrictions on how the money is used. The rationale for such restrictions is to portray the chosen policy areas as consistent with underlying EU objectives or (as is the case with agriculture and cohesion) to respect Treaty obligations. The trouble, though, is that in this logic, such policies can easily, and perhaps legitimately, be considered as EU public goods. In addition, where (as with the CAP) the spending goes to a coherent interest group, the lobbying power of such groups is likely to distort outcomes.

A second risk is that the distributive chapter risks entrenching, rather than countering, the juste retour reasoning that dominates Member State negotiating stances. There is an obvious incentive for net recipients to maximise

the distributive element and to play down the EU public goods, and vice versa for net contributors (especially if what is in the public goods chapter favours net contributors).

A third, consequent, concern is that disputes over what is distributive and what is a public good becomes a surrogate for juste retour negotiations. No spending programme is every entirely 'space blind' in the sense of conferring no advantage on any country or region. Even the location of public administration confers some gains on the regions that host the offices, while policies such as research (allocated on the basis of excellence) will tend systematically to benefit the (usually prosperous) regions where the best researchers are located.

Fourth, the size of the budget will be crucial. So long as the budget is capped at around its current level of around 1% of GNI, the scope for change will be limited not just by sheer inertia and its own history, but by the fact that any growth in spending in a particular area will imply cuts elsewhere or rapidly result in the budget reaching its political ceiling. In other words, the proposal put forward overlooks one of the trickiest elements of the political economy of the EU budget, namely that path dependency in what is spent is a major influence.

A further comment is that although the proposed matching of funding sources to chapters of expenditure can be presented as a neat way of respecting the Treaty commitment to fund the EU budget from own resources, Member States are unlikely to be fooled. Moreover, the proposal to have distinct funding flows may even distract attention needlessly from the underlying dichotomy between distributive (or equalising) transfers and spending on public goods. As is already the case, every finance minister can be expected to arrive at the negotiations armed with a spreadsheet pre-programmed with data on the incidence of conceivable taxes. Whether it is a variant on a carbon tax, modulated VAT or corporate income tax (to take three frequently advocated options) that is canvassed, there is bound to be some deviation from the ability to pay principle that the current GNI resource offers. Indeed, the current VAT resource had to be modified precisely because it was perceived to be unfair, turning it into a *de facto* GNI resource, and will probably now be discontinued.

Is this then a counsel of despair that nothing imaginative can be done? Certainly the EU budget has proved to be very resistant to change and is subject to a strong status quo bias. But instead of agonising over what is or is not a public good, an alternative to the Iozzo, Micossi and Salvemini approach may simply be to ask what sorts of EU spending would resonate with citizens and decision-makers. What, in short, would we really like the EU to spend its (that's to say *our*) money on?

There are many public goods for which a theoretical case can be made that the EU is the appropriate level to fund the required investments, but there will be inevitable differences of opinion about the supposedly objective criteria that should be used to rank them. The problem is, in addition, exacerbated by the political reality that the budget is unlikely to grow much from its current limited share of GDP and of aggregate public spending by all levels of government. The solution is to recognise that, instead, EU leaders need to make hard, politically based choices, that reflect political preferences as much as, if not more than, theoretically robust, but ultimately naïve abstract principles.

One emerging answer, as I have argued in a recent paper[1], is action to counter climate change. It is increasingly recognised that assuring a transition to a low-carbon economy will be a major challenge for the coming decades and that it will require substantial funding from the public sector. Analytically, a compelling case can be made that many of the necessary

1 Available for downloading at: http://www.eu-consent.net/content.asp?contentid=1789

investments – whether in new technologies, adaptation costs or infrastructure developments – are precisely the sorts of public goods that fulfil the criteria for elevation to the EU level. But what will count more is that this is the sort of EU spending that citizens can be persuaded makes sense. Similarly, today, citizens might look to the EU to do more to counter the economic downturn. In the past, even agricultural spending could be sold in these terms, although the political hard choices must also include when to end support for a policy.

Is it not worth a try?

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