THE MULTIANNUAL FINANCIAL FRAMEWORK AND THE FUTURE OF THE EUROPEAN UNION

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Abstract

This paper will look at the proposed Multiannual Financial Framework (MFF) for 2021-2027 and will explore how to achieve a better future for Europe through compliance with legally binding values and objectives of the EU: democracy, equality, the rule of law, economic, social and territorial cohesion and solidarity between the Member States. It is suggested that by introducing progressivity, a reform of the EU's finances, involving a change of paradigm in the financing of policies with redistributive effects, and a reform of the system of the EU's own resources could ensure that solidarity becomes a matter of the rule of law and not of arbitrary governance.

Key words

Multiannual Financial Framework, EU solidarity, rule of law, cohesion policy, progressive taxation.

Introduction

Presenting its package of legislative proposals for the next EU long-term budget – the Multiannual Financial Framework (MFF) for 2021-2027, the European Commission pointed out that there is an opportunity to unite around a clear vision for the future of Europe, that choices on the MFF 'will shape the Union for decades to come', and that a more united, stronger and more democratic Europe needs a new, modern budget.[107]

[107] European Commission, *A Modern Budget for a Union that Protects, Empowers and Defends. The Multiannual Financial Framework for 2021-2027*, Communication from The Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions. COM(2018) 321 final. Brussels, 2.5.2018.

This paper will examine the Commission's proposal for the MFF from the point of view of the Union's fundamental objectives, such as economic, social and territorial cohesion between the Member States, and values, such as equality, democracy, the rule of law and solidarity, and will explore how to achieve a better future for Europe by ensuring compliance with these legally binding fundamental objectives and values, which constitute the core of the social contract between the peoples of the EU, enshrined in the Treaties.[108]

1. The economic crisis and the values and aims of the European Union

The increase in *inequality* has been described as 'one of the *central* problems, facing the advanced world today'[109]. It has been recognized as the major negative consequence of globalization[110] and also of the economic crisis which recently hit the EU. Inequality is a central and therefore strategic challenge for the Union's future, relating to its fundamental values and aims. It concerns most directly the values of equality, solidarity and democracy in Article 2 of TEU and the aims of the economic, social and territorial cohesion among the Member States in Article 3 TEU.[111] According to Article 9 of TEU, equality is also the fundamental principle of democracy.

What was the EU's response to the economic crisis, what were the proposals for the Union's future and can these proposals ensure real convergence and effective cohesion among the Member States?

Following the Greek debt crisis, the European Commission's vision on completing Europe's Economic and Monetary Union, as expressed in the Five Presidents' Report[112], explicitly excludes 'permanent transfers between countries'. Such an attitude – in line with the neo-liberal economic thinking which

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[108] Consolidated versions of the *Treaty on the European Union* (TEU) and the *Treaty on the Functioning of the European Union* (TFEU) in: OJ C 202, 07.06.2016.

[109] Stiglitz, J. (2016), *The Euro and its Threat to the Future of Europe*, Penguin, p.260 – emphasis mine.

[110] See also: Stiglitz, J. (2012), *The Price of Inequality*, Norton, NY; Piketty, Th. (2014), *Capitalism in the Twenty-First century*. Harvard University Press.

[111] See also: Georgiev, D. (2017), *Inequalities and the Future of the European Union*. In: *The EU beyond 2020: in Search of Identity, Sustainability and Growth*. Bulgarian European Studies Association, Conference Papers, Sofia, 26 October 2017, pp.70-79; Георгиев Д. *Лисабонският договор и бъдещето на демокрацията в Европейския съюз*. сп.Юридически свят 2/2016, с.68-95.

[112] European Commission. *Completing Europe's Economic and Monetary Union. Report by: Jean-Claude Juncker in close cooperation with Donald Tusk, Jeroen Dijsselbloem, Mario Draghi and Martin Schulz*. 22 June 2015, p.15.

rejects redistribution for the overcoming of economic and social inequalities – is not compatible with the fundamental objective of cohesion between the Member States and constitutes a major risk for the future of the EU. The Treaty on the Functioning of the EU in its Article 175 does provide for the financing of economic, social and territorial cohesion through its Structural Funds, the European Investment Bank and its other existing financial instruments. Moreover, Article 175 of TFEU requires that the internal market and all the policies and actions financed by the Union contribute to the achievement of the objectives of economic, social and territorial cohesion.

Although the Commission's White Paper on the Future of Europe[113] starts with the famous reference to solidarity in the Schuman Declaration[114], neither the White Paper nor its reflection papers propose concrete ideas on setting up effective mechanisms for real economic and social convergence and genuine solidarity among all Member States. The scenarios proposed envisage instead the possibility of a multispeed Europe with 'coalitions of the willing' consisting of certain Member States only – those that 'want more and do more'. Even at first glance it is quite obvious that such a scenario cannot guarantee the reduction and elimination of economic and social imbalances and inequalities among *all* Member States and cannot be the starting point of a targeted reform of the EU's economic policies so as to bring these policies in compliance with the fundamental values of equality and solidarity and fulfil the Union's objectives of convergence and of economic, social and territorial cohesion.

What was proposed for the euro area specifically was, *inter alia*, tax harmonization and new agreed social standards. But harmonization of corporate taxation cannot lead to reducing the economic inequalities between the Member States because it would deprive the less advanced ones of the possibility to attract investment by offering tax incentives whereas imposing high social standards could lead to rising costs of production and a decrease in their competitiveness. The result would be lower growth in the Member States with a lower level of development and less real convergence and less cohesion in the euro area and in the EU as a whole. One could strongly doubt that aligning Member States' business taxation frameworks with the proposed Common

[113] European Commission. *White Paper on the Future of Europe. Reflections and scenarios for the EU27 by 2025*. COM(2017)2025 of 1 March 2017.

[114] 'L'Europe ne se fera pas d'un coup, ni dans une construction d'ensemble: elle se fera par des réalisations concrètes, créant d'abord une solidarité de fait' (Declaration Schuman, 9 mai 1950)

Consolidated Corporate Tax Base, as envisaged by the reflection paper on the EMU, would 'help to drive convergence by facilitating cross-border trade and investment'. The proposal for a separate euro area budget with a stabilization function but without transfers in the form of automatic progressive stabilizers could have an even stronger negative effect on real economic convergence in the EU as a whole. Even its effect on convergence between euro area members only is doubtful, given the experience so far, with the euro serving as a factor of divergence rather than of convergence. Divergence and inequalities are generated, as a result of the EU's economic and monetary policies and the internal market, not only within the euro area but also between Member States in the whole of the EU. Therefore, measures of solidarity to reduce and eliminate economic and social disparities and inequalities need to be taken in the whole of the EU. This is true not only of economic or monetary policies but also of all other internal and external policies of the Union, especially the ones with significant distributive effects, including those funded entirely or partially from the EU budget. And, as Article 326 of TFEU stipulates that enhanced cooperation 'shall not undermine the internal market or economic, social and territorial cohesion', the 'coalitions of the willing', as envisaged in the White Paper, may be in breach of the EU primary law and the fundamental values of equality and solidarity.

The main flaw of the scenarios of the White Paper and the reflection papers of the Commission was that they ignored the centrality of inequality and divergence as fundamental problems of the EU and that, by diverting attention to the external challenges facing the Union, they disregarded the potential role that strategies for the effective reduction and elimination of inequalities between the Member States can play for the solution of these problems and challenges.

This flaw also persists in the package of legislative proposals of the Commission for the new MFF. The Commission's proposal on the system of 'own resources'[115] does not aim at reducing the regressive[116] and unequitable character of the Union's revenues system. Rather than proposing to eliminate the regressive elements of the 'own resources' system (such as the reductions or ceilings of the GNI- and VAT-based contributions by Member States) and to abolish the VAT-based contribution by Member States, it in-

[115] European Commission, *Proposal for a Council Decision on the system of Own Resources of the European Union.* COM(2018) 325 final, Brussels, 2.5.2018.

[116] Monti, M. *et al.*, *Future Financing of the EU, Final report and recommendations of the High Level Group on Own Resources*, European Commission, Brussels, December 2016, p.8.

tends to reinstate the reductions (due to expiration in 2020) for some Member States with a high GNI per capita and introduce a revised version of the VAT-based contribution. In addition, the Commission proposes new categories of own resources with the intention of reducing the share of GNI-based contributions by Member States, which are admittedly[117] the most equitable own resource of the EU revenues system. Thus, the proposals would make the system of the EU revenues more regressive and less fair.

On the expenditure side, regarding the financing of the various sectoral policies, such as the common agricultural policy, regional policy, etc., it seems that the Commission, here too, has not been guided by the objectives of cohesion and the fundamental values of equality and solidarity and the Treaty requirement of Article 175 of TFEU that all policies and actions 'shall contribute' to the achievement of cohesion, but by an attempt to ensure '*juste retour*' and to avoid 'permanent fiscal transfers'.[118] These are considerations which are not based on the EU Treaties, i.e. the existing 'social contract' between the peoples of the EU, which are not compatible with the Union's fundamental objectives and values and which constitute a major risk and threat for the future of this social contract.

The proposal for the new MFF and the rule of law

The package of legislative proposals for the next MFF of the European Commission includes a proposal for a regulation 'on the protection of the Union's budget in case of generalized deficiencies as regards the rule of law in the Member States'.[119] This proposal envisages introducing a procedure whereby the Commission would be able, if 'it has reasonable grounds to be-

[117] Ibid., pp.7, 12, 37.

[118] It is rather disappointing that some of the visions for the future of the EU presented on the occasion of the elections to the European Parliament in 2019, including some supported by prominent contemporary intellectuals who declare themselves 'pro-European', in reality fail to comply with the values and objectives of the EU. Thomas Piketty, for example, who in his outstanding work on capitalism in the 21st century has underlined the role that 'modern redistribution' can play for the elimination of economic inequalities, proposes a new Treaty (of the Eurogroup and 'those who want to advance') with progressive taxation but without any 'financial transfers', i.e. without redistribution and cohesion among the Member States and without the prospect for real equality among *all* citizens and *all* peoples of the EU.

[119] European Commission, *Proposal for a regulation of the European Parliament and of the Council on the protection of the Union's budget in case of generalised deficiencies as regards the rule of law in the Member States*. COM(2018) 324 final, of 2.5.2018

lieve' that there are 'generalised deficiencies as regards the rule of law' in a Member State, to adopt measures, including suspension of payments to Members States, reduction of funding, prohibition to conclude new commitments. These measures 'shall be deemed to have been adopted by the Council unless it decides, by qualified majority, to reject [them] within one month of [their] adoption by the Commission'. The proposal, which is obviously meant to overcome the 'inefficiency' of the mechanism for protecting the values of the EU in Article 7 of TEU, in fact, aggravates the deficiencies of the procedure in terms of the rule of law[120] – the value which it claims to protect.

A major deficiency with respect to the rule of law which would result from the Commission proposal is that the Commission, an executive body of the EU, not accountable democratically to any national body, and with a deficit of democratic legitimacy in the EU, would be given the power to pass judgements, without being a court, about any 'widespread or recurrent practice or omission, or measure' of any national public authority, even of democratically elected national legislations. Thus, the Commission would be in a position to exert political pressure and interfere in national legislation and decision-making, i.e. in the domestic democratic political process, on matters beyond the EU competencies.

If adopted, this proposal would enhance the already immense discretionary power of direct governance of the Commission. As it is not about placing power under superior rules, principles or values, it can hardly be claimed that it is about protecting the rule of law in the EU itself. It is about placing the power of the Member States under the power of the Commission and enhancing this power to new proportions and thus, rather than protecting the rule of law of the EU, the proposal would result in its erosion. If the proposal is adopted, the EU would be taking a step further away from democracy and a step closer to becoming an 'empire'.

What can be done to protect the values of the EU and to ensure the promotion of its objectives in the new MFF?

If the Member States want to bring more rule of law in the Union's finances, they would have to introduce more rules and principles into its

[120] Georgiev, D. (2019), *The Rule of Law and the EU Budget for 2021-2027: More Solidarity or Renouncing the Values of the EU?* Środkowoeuropejskie Studia Polityczne, 2/2019.

budget and its policies and leave fewer possibilities for arbitrary political decisions by the executive bodies and fewer possibilities for *ad hoc* decision-making and for political pressure and bargaining. If they want to make the EU more democratic, they would need to reform the finances of the EU, especially the financing of the various policies of the EU, so as to bring them also in conformity with the value of equality as a fundamental principle of democracy and with legally binding objectives, such as economic, social and territorial cohesion and solidarity between the Member States.

A reform of the finances of the EU ought to ensure that those who benefit more from the Internal Market and its policies also contribute more financially and that more cohesion assistance is directed to those who need it more. Redistribution at the level of the EU and through the EU budget is the key to tackling economic inequalities between Member States and achieving a level playing field for all. Central to reducing inequalities in the EU and making it more democratic by means of more solidarity and more rule of law would be to transform the EU's own budgetary system, which is now regressive[121], into a *progressive* one. As Galbraith points out, 'For a good society, a more equitable distribution of income must be a fundamental tenet of modern public policy and to this end progressive taxation is central.'[122]

Introducing progressive taxation in the EU by obliging Member States to harmonize their national tax laws is, however, not desirable at this stage as it would be counter-productive. It would have negative consequences for the competitiveness of the economically less advanced Member States and would not lead to more investment, economic growth and accelerated economic, territorial and social cohesion but, on the contrary, to further legal consolidation of the economic inequalities between and within Member States. As long as the EU is composed of separate economies that are in competition with each other and there is no common EU social system based on genuine solidarity and as long as each Member State is responsible for its own taxation and budget, the introduction or not of progressive national taxation, as well as national internal distribution and redistribution and social policies, should remain the competence of each Member State. Unless the EU builds a common social system based on solidarity and funded at the EU level, it will not have sufficient democratic legitimacy to impose social stan-

[121] Monti, M. *et al.*, *Future Financing of the EU, Final report and recommendations of the High Level Group on Own Resources*, European Commission, Brussels, December 2016, p.8.

[122] Galbraith, J.K. (1996), *The Good Society: The Humane Agenda*, NY, p.65.

dards on Member States and to intervene in domestic redistribution matters, including in taxation and in social legislation.

The EU can bring more justice to its redistributive system, its policies and its budget not by harmonizing Member States' tax laws but by introducing progressivity in the Union's own finances. For a reform of the EU's own revenues and of the EU distributive policies to be effective, it needs to be comprehensive so as to fulfil the condition of Article 175 of TFEU which requires the internal market and *all* of the Union's policies and actions to contribute to the achievement of the objectives of economic, social and territorial cohesion.

Such a comprehensive reform, necessary to effectively achieve the objectives of cohesion and of democratization, is not envisaged in the package of legislative proposals of the Commission for the MFF 2021-2027. The package consists of different proposals for legislative acts on the financing of the various policies, which will be adopted separately, most often with the ordinary legislative procedure which requires a qualified majority vote in the Council. So, if the Member States interested in a comprehensive reform manage to organize as a sufficiently numerous[123] group, they could try to introduce separate elements of progressivity in the financing of the various policies.

What could those elements of progressivity be in the various policy areas?

On the *revenue* side, in the Union's system of 'own resources', progressivity could be introduced for the Member States' contributions based on Gross National Income (GNI) with a coefficient which would reflect the percentage of deviation of the respective Member State from the EU average GNI per capita. It would also be important to eliminate all other regressive elements of the present own resources system, such as the VAT-based contribution by Member States.

In the present system[124] the main regressive elements are the permanent correction mechanism in favour of the United Kingdom and the temporary (2014-2020) reductions in the GNI- and VAT-based contributions of some Member States with high GNI per capita. The latter will expire before the next MFF. For the next MFF the Commission proposes[125], however, to re-

[123] The Council, under Article 241 of TFEU, 'acting by a simple majority, may request the Commission to undertake any studies [which it] considers desirable for the attainment of the common objectives, and to submit to it any appropriate proposals'.

[124] Council Decision of 26 May 2014 on the system of own resources of the European Union, (2014/335/EU, Euratom)

[125] European Commission, COM(2018) 325 final, Brussels, 2.5.2018.

install the reductions in the annual GNI- and VAT-based contributions for 2021-2025 for the Member States which have them now. In addition, the Commission proposes three new 'own resources' (based on a common consolidated tax base, on the EU emissions trading system and on plastic packaging) the principal purpose of which is to replace part of the GNI-based contributions of Member States. As has been shown above, reducing the share of the GNI-based contributions would not make the system less regressive and more equitable.

A decision on the Union's 'own resources' would require unanimity in the Council and a strong resistance could be expected to an introduction of a progressive coefficient and to the elimination of VAT-based contributions. On the other hand, unanimity is a guarantee against attempts, such as those of the Commission, to make the EU's revenue system more regressive. Therefore, Member States which are interested in making the EU's own resources system more equitable should not hesitate to oppose any such attempts.

Also on the *revenue* side, when concluding free trade agreements with third countries which GNI per capita is above the EU average (including agreements under Article 50 of TEU on withdrawal from the Union), arrangements should be made for contributions to the EU budget by such countries, as is the practice with other European non-EU Members.

On the *expenditure* side, i.e. regarding the financing of EU policies, various instruments could be used to introduce progressivity, including coefficients based on the deviation from the EU average GNI per capita, national co-financing, other 'progressive automatic stabilizers'[126]. For the majority of policies and programmes, most suitable would be a combination of EU funding and national co-financing, respectively increasing and decreasing proportionally to the deviation of the given Member State from the EU average GNI per capita. The aim would be to offset the unfair regressive character of the own resources system whereby Member States with lower GNI per capita contribute to policies more beneficial to Member States with higher GNI per capita.

Cohesion funding from the EU budget, for example, should be available only to Member States with a per-capita GNI of less than 90% of the Union average, as required by Protocol (No 28) on economic, social and territorial cohesion. For regional aid, national co-financing could be set at a very low level for Member States with a GNI per capita below a threshold (e.g. of 75

[126] Stiglitz, J. (2016), *The Euro and its Threat to the Future of Europe*, Penguin, p.247

% of the EU average) and could increase progressively to a very high level (e.g. up to 99% of the respective amount of the total financing) for Member States with a GNI per capita above another threshold (of e.g. 110% of the EU average GNI per capita).

Similarly, the financing of the EU Common Agricultural Policy, which still accounts for a large part of EU expenditure, could be made to comply with the requirements of Article 175 of TFEU by introducing national co-financing[127] only for Member States with GNI per capita above the 90% cohesion threshold and below some other threshold, e.g. 110% of the EU average GNI per capita, while Member States with a still higher GNI per capita, who would not receive any EU funding, could be allowed to give subsidies from their national budgets only up to levels which would not undermine the competitivity[128] of farmers receiving EU aid in other Member States.

The EU cohesion funding could be made available not only for infrastructure and environmental projects, but also – and above all – for investment in, and development of, production capacities for goods and services with high added value, and for creation of local jobs in the most underdeveloped regions. Such aid is particularly effective as it ultimately makes itself unnecessary.

On investment, for programmes like the 'Juncker Plan', funding from the EU budget could be reserved for projects in the economically less advanced Member States only and the amounts from the EU budget available to each Member State could reflect its deviation from the EU average GNI per capita and could be fixed in advance in the MFF so as not to depend on discretionary decisions by the Commission or other bodies. The European Investment Bank (EIB) and other EU financial facilities could give preferential loans and guarantees for projects for developing less developed regions (which is the EIB's first task under Article 309 (a) of TFEU), ensuring a fair distribution between the Member States.

The EU funding for social programmes could be made available only for Member States with a GNI per capita less than the EU average and the amounts allotted to Member States would reflect their deviation from the EU average.

A comprehensive reform, aimed at adjusting the financing of the Union's policies to its fundamental values and objectives, should also include an ad-

[127] National co-financing – to match the lower agricultural subsidies from the EU budget – was allowed for the new Member States during the first ten years of their membership.

[128] For that it would be necessary to have identical maximum direct subsidies per hectare in all Member States.

justment of its competition policy. It could be decided, for instance, by using the procedure in Article 107.3(e) of TFEU, that aid granted to the economy of any Member State with a GNI per capita less than a certain percentage of the EU average (e.g. 90%) shall be compatible with the internal market.

Generally, in a comprehensive reform of the Union's finances of *all* policies and programmes, fair distribution of EU funding could be ensured by using clear, fair and transparent formulae analogous to the ones mentioned and which could be applied automatically, as 'progressive automatic stabilizers', rather than based on case-by-case discretionary decisions by EU bodies or reached through political bargaining between Member States. In order to comply with the value of the rule of law, there should be no discretionary decisions by the Commission or by other bodies on the distribution of funding between the Member States. The allocations of EU funding between the Member States (or beneficiaries from the Member States) should be fixed in advance, both for the various programmes and overall, for the whole MFF, and there should be no 'flexibility' to move funding between Member States. Funding not used by a Member State should not be returned to the EU budget, but should remain available to the respective Member State in the next budgetary period and for other policies or programmes.

In the debate on the financing of policies related to migration – a politically controversial matter – there is the perverse view on solidarity as a 'two-way street', implying that Eastern and Central European Member States, which receive cohesion money, should in exchange pay in case they refuse to host migrants[129]. It would be difficult to make an assessment what a fair system of financing migration would be without taking into account all elements of that system, in particular, which Member States should be responsible for hosting migrants. Now it is the first Member State where the migrant entered EU territory, but in most cases this is not necessarily the country where the migrant wants to go and it is proposed that this should be changed. Compulsory resettlement cannot be described as fair either to migrants or to Member States which do not want to host migrants. *Prima facie* it would appear that in a system with a freedom of movement of people, such as the EU claims to have, EU money should go with the migrant freely moving in the EU. With an overall regressive EU financial system this would, however, mean that poorer Member States would be paying to richer Mem-

[129] Euractiv.com with Reuters, *Host migrants or pay, France and Germany propose*. 7.12.2018.

ber States to host migrants, which – at least theoretically – would, in the long term, help to boost the economies of those richer countries. Such a system would, therefore, be highly unfair to the poorer Member States. In this situation the new MFF could envisage, on the one hand, to discontinue payments of EU funds related to hosting migrants to Member States with a per-capita GNI higher than the EU average (or higher than a threshold related to the EU average – e.g. the cohesion threshold of 90%). On the other hand, it could be made financially attractive for the Member States below that threshold to host migrants – if they are willing to do so – by giving them much more than they would actually spend on each migrant, in order to strengthen the social security systems for their own citizens.

A separate EU budgetary policy for the euro area, as advocated by some[130], especially one 'focused mainly on investment and convergence', that provides solidarity and automatic and discretionary stabilizers not within the EU as a whole, but for the euro area only[131], would, of course, lead to further deepening of the divergence with those countries outside the euro area which need it most. Since burdens, disadvantages and inequalities do not arise uniquely as a result of the functioning of the euro area itself, but within the internal market as a whole, having a separate budget for the euro area, especially for investment, would be in breach of fundamental values and objectives of the EU, such as solidarity and cohesion.

Conclusion

If the EU does not undertake an effective reform of its redistributive policies to ensure that progressivity and solidarity in the EU become a matter of the rule of law and not of governance through conditionalities and fines, in the foreseeable future the Union will bear less and less resemblance to a democracy and will increasingly look like an empire with an economically stronger and more rapidly developing 'core' and an economically weaker 'periphery' in the East and the South, lagging behind the 'core'. The challenge for the future of the EU is to succeed in reforming the system of the financing of its policies, so that they comply with the values of democracy, equality, the rule of law and solidarity and with the objectives of economic, social and territorial cohesion among Member States.

[130] Habermas (2018).

[131] Rios B., *Eurozone budget to be ready by 2021 say France and Germany* – Euractiv.com, 20.11.2018.

Although such a reform of the EU's finances would boost the well-being of the citizens of the Union as a whole and would, therefore, be in the interests of all, immediate political support for such a reform – in the course of adoption of the legislative proposals for the MFF 2021-2027 package – in the Council is not likely. Therefore, what is needed is collective action by the Member States most immediately interested in such a reform. It would take the ability of these countries to join efforts, organize as a group and act collectively at all levels – at the level of the European Council, in the different Council formats and in the European Parliament – to defend their interests in the course of the adoption of the legislative proposals for the next MFF.

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