The Multiannual Financial Framework

The search for flexibility and recognised effectiveness

Adriaan Schout
Luuk Molthof
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Clingendael Report

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Executive summary

The European Union (EU) is currently confronted with developments that could have deep impacts on our societies and policies. Yet the EU's Multiannual Financial Framework (MFF) – which defines the size and aim of the EU budget over a certain period of time – has difficulties in overcoming its inflexibility and ensuring best value in relation to shifting priorities. One important step that could modernise the MFF would be to improve the use of effectiveness assessments in relation to EU spending.[1]

In 2003, André Sapir and colleagues famously referred to the MFF as a 'historic relic' with expenditures, revenues and procedures being 'inconsistent with the present and future state of EU integration'.[2] Although the MFF has improved since then, it continues to suffer from discrepancies between stated priorities and actual spending. EU finances risk becoming increasingly reliant on funds and instruments outside the MFF ceiling because existing programmes are hard to change. Moreover, doubts about the effectiveness of the MFF remain.[3]

With European integration having moved far beyond the level of technical harmonisation of the internal market, the EU budget, arguably, needs more flexibility to respond to current geopolitical and societal challenges and investment needs. As political discussions on the next MFF – the current MFF runs from 2021 to 2027 – are starting, this report discusses avenues for realigning expenditures to changing EU priorities and to unforeseen challenges and crises.

1 With the focus on effectiveness, this report concerns 'performance audits'. The International Organization of Supreme Audit Institutions (INTOSAI) makes a three-way split in monitoring tasks: financial audits (auditing financial information); compliance audits (auditing the compliance of the activities); and performance audit (examining the room for improvement in terms of economy, efficiency and effectiveness). See INTOSAI, 'Fundamental Principles of Public-Sector Auditing', 2019, section types of public audit, page 11.

2 André Sapir, et al., 'An Agenda for a Growing Europe: The Sapir Report', Oxford University Press, 2004, p.162,

3 See e.g. Torben M. Andersen et al., 'It's OK to Be Different: Policy Coordination and Economic Convergence', CESifo, 2018; Adriaan Schout and Arthur van Riel, The state of economic convergence in the Eurozone. Two decades of monetary union and economic governance, January 2023

In order to enhance flexibility suitable procedures are required that would lead to political decisions based on accurate assessments. Furthermore, better methods are needed to communicate potential – and possibly painful – shifts in priorities to the broader public. In order to develop such procedures, thorough analysis and discussion are needed on the effectiveness of EU programmes and the use of effectiveness assessments in redefining political priorities.

This report therefore relates the concept of European added value – defined by the Commission as 'the value resulting from an EU intervention which is additional to the value that would have been otherwise created by Member State action alone' – to mechanisms to better respond to new situations.[4] One of the questions this raises is whether the current (multilevel) systems for assessing European added value are able to offer the timely information needed for flexibility. Given the workload involved in performance assessments, and given the importance of national ownership of reforms, further analysis is needed of the role of the European Court of Auditors (ECA) and its interactions with its national counterparts.

This report makes the following recommendations:
1. Any shortening of the MFF's duration could improve the EU's ability to respond to changing priorities. Yet rather than focusing on the length of the budget cycle – a discussion that is ongoing – it is advised to focus instead on the length of programmes under the MFF (some may run for three years, others for ten).[5]
2. Flexibility can be explored through working with sunset clauses – meaning that programmes cease to be effective after a specific date unless further action is taken. The use of such clauses should be tied to requirements for independent assessments of the European added value before decisions on

4 European Commission, "Commission staff working paper, The added value of the EU budget", 29 June 2011, p.2; Peter Becker, "Budgeting as the political creation of added value", *ECA Journal*, 2020, nr.3, p.34-37.
Yuri van Loon and Adriaan Schout, "European Added Value narrows EU budget reform discussions", Clingendael, February 2018.

5 The discussion on shortening the current length of the budget cycle to, for example, five years is ongoing. We want to stay clear of this discussion and focus instead on ways to improve the link between the multiannual budget (whatever length it may have) and the effectiveness of programmes under the MFF.

prolongation are taken. This may help to sharpen political discussions on reprioritisation.

3. The financing of the MFF via the national contributions, based on a specific percentage of gross national income (GNI), is a fair and efficient foundation for the EU budget. The GNI principle also ensures that money is scarce: priorities have to be matched with the existing contours of the EU budget. This serves the efficiency of the budget and helps to focus attention on EU added value (the effectiveness of the budget).
4. A fixed percentage of GNI could help to recommit to the scarcity principle in the budget and could help to prioritise expenditure in line with EU objectives. More important than the actual amount of this percentage, however, is whether decisions on the selection of programmes are based on effectiveness assessments. The GNI contribution could possibly be increased if linked to a deeper use of independent effectiveness assessments.
5. Assessment of the European added value of the EU budget demands a reconsideration of the current audit mechanisms in terms of their timing, lessons learned, and subsidiarity-based ways of working when it comes to pan-European assessments of effectiveness.[6]
6. Provided that independent assessments and their use are improved, the European perspective in the MFF could be further reinforced through more fundamental reforms such as introducing Qualified Majority Voting (QMV) in the Council in revising the MFF and extending the powers of the European Parliament through co-decision in the adoption of the MFF.

These actions would result in a reform package aimed at strengthening European added value (and hence flexibility) combining a fixed percentage of GNI and effectiveness assessments of spending before political decisions are made on prolongation of programmes. Given the starting point that money is scarce, this package will produce considerable political heat over the use of the EU budget. This heat can be considered as part of normal politics regarding budgets.

Such reforms will involve serious discussions and demand considerable time. It is nevertheless worthwhile to put them on the agenda to explore new directions in the move away from the current inflexibility and *juste retour*. *Juste retour* – which implies the net budgetary balance that simply compares a member state's

6 Adriaan Schout, "EU Subsidiarity as an Antidote to Centralisation and Inefficiency", Brussels: Martens Centre, 2022.

financial contribution to the EU budget with the money that flows back into the country – is a misleading indicator of the benefits of EU spending. Rather, this reform package would support assessments-based budgetary decisions that contribute to the *European* added value of the budget.[7]

7 Magdalena Sapala, "Strengths and Weaknesses of the EU Budget Flexibility 'toolbox'", in in Brigid Laffan and Alfredo De Feo (eds.), *EU financing for the next decade. Beyond the MFF 2021–2027 and the Next Generation EU, European Union Institute*, 2020, p.259.
Margit Schratzenstaller, "The next Multiannual Financial Framework (MFF), its Structure and the Own Resources", *FairTax Working Paper Series*, no.14, November 2017.

1 Introduction: the challenge of flexibility and effectiveness

With a large share of expenditure pre-allocated to traditional priorities, such as agriculture and cohesion, and locked in for a period of seven years, the EU's current Multiannual Financial Framework (MFF) – which defines the size and aim of the EU budget for a seven year period from 2021 to 2027 – is not well equipped to respond to new challenges and crises.[8] There is a current tendency to address new challenges through additional funds arranged outside the MFF. During the Covid-19 pandemic, for example, a new instrument was created to support member states' economic recovery from the crisis. This Next Generation EU (NGEU) package – with its Recovery and Resilience Facility (RRF) of €750 billion worth of grants and loans for reforms and investments – came on top of the EU's long-term budget (€1,074.3 billion – at 2018 prices).[9] The somewhat shorter duration of the NGEU implied, approximately, a doubling of the EU budget without a thorough re-examination of existing spending programmes.

Since the adoption of the Global Strategy in 2016, defence spending is increasingly becoming a serious financial issue for the EU and its member states. This trend has intensified since the Russian invasion of Ukraine in 2022.[10] Energy scarcity and the reorientation of energy sources have added to the political pressures on the EU budget.[11] Similarly, major investments in the green and digital transitions, and, among developments, the response to Biden's Inflation Reduction Act (IRA) in the form the of Green Deal Industrial Plan, have triggered debates over new resources.

8 Giacomo Benedetto, "A new package for finance and expenditure in the EU budget", *European Parliament*, March 2020, p.2.

9 https://www.consilium.europa.eu/media/47296/1011-12-20-euco-conclusions-en.pdf.

10 Dick Zandee, *Open strategic autonomy in European defence: what countries must do*, Clingendael Policy Brief, 2022

11 Giacomo Benedetto, "A new package for finance and expenditure in the EU budget", *European Parliament*, March 2020, p.2.

The European Peace Facility (EPF), in particular, is an example of a financial programme outside the EU budget that is struggling to keep up with new realities.[12] The EPF, introduced in March 2021 to enhance the EU's ability to promote global security, has the hallmarks of an additional budget that gets increasingly complicated as its purpose and size increases.[13] Furthermore, the EPF is a crisis fund initiated as an intergovernmental instrument but administered by the Commission. Therefore, the supervision and audit arrangements are outside of the EU framework (and outside the brief of the European Court of Auditors (ECA)).

Geopolitical dynamics necessitate a reassessment of current decision-making procedures over the EU budget and related performance assessments. Dealing with new challenges apparently cannot be done through reorientation within existing financial and procedures frameworks. The ECA published a report on the EU's financial landscape addressing the many oversight arrangements.[14] In addition to the multiplication of budgets, the auditing of the effectiveness of EU programmes is not connected to the political priorities of the Commission. In fact, political discussions on the MFF, and much of the literature on the EU budget, focus on decision-making procedures and priority setting, while surprisingly little attention has been devoted to the role of (performance) auditing. This limits the possibility of informed debates about reorientations within the budget.

Negotiations over the EU's multiannual budget have traditionally been driven by net balance considerations, so-called *juste retour*.[15] Doubts about European

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12 Reuters, EU states to top up fund used for Ukraine arms purchases by 2 bln euros. 8 December 2022, accessed 21 March 2023.

13 Central European Times, EU clears path for EUR 18bn loan to Ukraine - CET (centraleuropeantimes.com), 11 December 2022, accessed 21 March 2023.
Dutch Parliament has some concerns about the accountability process of the European Peace Facility. Concerns over the accountability of the intergovernmental EPF resulted in two Motions in Dutch Parliament. Motions in Dutch Parliament. https://www.tweedekamer.nl/kamerstukken/moties/detail?id=2022Z25047&did=2022D53892 and https://www.tweedekamer.nl/kamerstukken/moties/detail?id=2023Z02152&did=2023D05046.

14 ECA (2023), *The EU's financial landscape – A patchwork construction requiring further simplification and accountability*. Luxembourg: special report 05/2023. https://www.eca.europa.eu/Lists/ECADocuments/SR23_05/SR_EU-financial-landscape_EN.pdf

15 Bertelsmann Stiftung (2013), "The European Added Value of EU Spending: Can the EU Help its Member States to Save Money?". Jean Pisani-Ferry, "A radical way out of the EU budget maze, European Council on Foreign Relations", *European Council on Foreign Relations*, 26 February 2020.

effectiveness may have sharpened the defence of national returns and these doubts were likely reinforced by the lack of – timely – information on actual results in terms of EU added value.[16] Spending programmes are large and cumbersome to assess in terms of performance, and assessments tend to come after decisions on programme continuation have been made (see below). If European added value (i.e. effectiveness) remains opaque, member states may as well go for *juste retour.*

In general, in an EU and international arena that has become much more dynamic compared to the more limited use for which the EU budget was initially designed, effectiveness of – and public support for – spending programmes can easily become an issue. This is not to say that no effort has been made to improve the long-term budget's added value and flexibility. The 2021-2027 MFF included changes that arguably improved the budget's added value and agility. For instance, more funding was devoted to research and innovation, and migration and border control,[17] and stronger emphasis was placed on the twin transitions (greening and digitalisation).[18] Yet doubts remain over the European effectiveness of considerable parts of the MFF and its overall flexibility.

The 2021-2027 package introduced some additional instruments to allow for unforeseen expenditures.[19] However, due to the Russian invasion of Ukraine, the (ensuing) energy shortages, and the subsequent high levels of inflation, the budget is under pressure. As a result, extensive use has already been made of the additional instruments in the first two years of the MFF.[20] This has led to calls for new programmes and continuation of recently agreed temporary finances (loans-based programmes).

16 Adriaan Schout and Arthur van Riel, 'The State of Economic in the Eurozone', Clingendael January 2023; See also Barone, G., G. de Blasio (2023), Place-based policies in the Italian case, part 1: A lot of money for little or no growth, CEPR, 2023

17 European Council, "Multiannual financial framework for 2021-2027 adopted", 17 December 2020; Ministry of Foreign Affairs. "Raad en Europees Parlement stemmen in met MFK 2021-2027", 11 January 2021.

18 Europa Nu, "Europees financieel kader 2021-2027", accessed 18 January 2023.

19 The Flexibility Instrument; The Single Margin Instrument; the Brexit Adjustment Reserve, the European Globalisation Adjustment Fund and the Solidarity and Emergency Aid Reserve. For an overview see: Flexibility and special instruments (europa.eu).

20 European Parliament, "Draft Report on upscaling the 2021-2027 multiannual financial framework: a resilient EU budget fit for new challenges", 16 September 2022, p.10.

This report looks ahead to the next MFF. How can the flexibility and effectiveness of the next EU budget be enhanced as compared to the current one? What measures could the Netherlands propose in the EU arena to ensure that, by the end of this decade, the EU has a modern budget able to tackle the major transitions of the near future? Based on analyses of policy reports and interviews, it reflects on potential avenues for improving budget flexibility, added value, and (financial) sustainability. As any reform of the EU budget would demand compromises, we look not only at the expenditure side of the budget, but also the revenue side (in particular the GNI basis for financing the MFF). Considering the fact that repayment of NGEU debts has not yet been fully resolved – with repayments starting in an undefined way in 2028 – negotiations over the MFF are likely to be especially complicated as countries may have incentives to avoid cuts in existing programmes.

Although the Commission's proposals for the next MFF are only due in summer 2025, it is imperative to start weighing options for further modernising the budget in the light of current challenges, increasing public awareness and acceptance, and securing Europe's earning power. Special attention will be paid to the question of how the Dutch government, which has traditionally been an advocate of reforming the budget, could position itself in the discussions. Is a reform package possible that enhances the impact of the EU's finances by focusing the budget on current and shifting political priorities while avoiding head-on confrontations over the politically sensitive programme headings (for the headings, see Table 1)?

This report is divided into two sections. The first section provides insights into the essential context by briefly elaborating the history, structure and composition of the EU's long-term budget. It reflects on the decision-making process and the various positions in the negotiations, and it provides an overview of the current MFF, identifying strengths and focal points for reform. Starting from a concern for effectiveness audits, the second section explores possible options for realigning expenditure to new EU priorities, enhancing the budget's adaptability to unexpected challenges and crises, securing financial sustainability of the budget and making added value transparent to the wider public. In order to guide (political) discussions in the run-up to the negotiations for the next MFF, this section includes key questions and points for discussion.

2 The EU budget: composition, negotiations and recent changes

The EU's multiannual budget essentially determines the direction of EU policy for a period of at least five, but usually seven, years. It sets the political priorities for the given period and the maximum sums that can be spent each year per category (see the headings in Table 1). The *Own Resources Decision* defines how the EU budget is financed (Art 311 on the Functioning of the European Union). Through the introduction in 1988 of multiannual budgeting, the EU budgetary process gained in certainty and predictability[21] while avoiding complex recurrent negotiations; however, it lost in terms of flexibility.[22]

In practice the 7-year budget cycle implies a 13-year timespan. The proposal for the MFF is drafted approximately two years before the next cycle. The finances can be used up to three years after the MFF (the eligibility period) while the spending stops one-and-a-half years after the ending of the eligibility period.[23] Furthermore, assessments and lessons drawn from programme evaluation will often only be available during the running of the next MFF. As a corollary, the assessments will have an influence on the MFF five to seven years after the previous MFF is closed.

2.1 Size and composition

By far, the main contribution (70%) to financing from the EU budget comes from national contributions, based on a specific percentage of gross national income (GNI) of the EU member states. Smaller contributions result from the *value*

21 For the official history of the EU Budget, see Publication Office of the European Union, *European Union: Public Finances*. European Union public finance - Publications Office of the EU (europa.eu)

22 European Commission, "The evolving nature of the EU budget", *EU budget policy brief*, October 2021, p.7.

23 European Court of Auditors, 'EU budget: time to reform? A briefing paper on the mid-term review of the Multiannual Financial Framework 2014-2020', 2016.

added tax, and, since 1 January 2021, a *plastics own resource*.[24] The *GNI-based own resource* has tripled in absolute terms since the late 1990s, and its relative contribution to the budget has also increased substantially since then (from 40% to 71% in 2020).[25]

In terms of process, the budget is a compromise between multiple interests and rationales. Agriculture and cohesion policy have traditionally taken up a large share of the EU budget and, due to vested interests, changes in prioritisation are difficult to implement. Yet, 'European added value' has emerged as a central – although somewhat elusive – concern. At its heart, the concept is closely linked to subsidiarity, as illustrated in the European Commission's definition: 'European added value is the value resulting from an EU intervention which is additional to the value that would have been otherwise created by Member state action alone.'[26] The Commission envisions that the concept is used as a 'key test to justify spending at the EU level'.[27] In theory, EU added value should underline the European character of the budget.

Although agriculture and cohesion have declined over the years, they still make up over 60% of the MFF. Due to changing environmental, social, economic and (geo)political circumstances, other priorities have been brought to the fore. Yet the 'newer' priorities are only slowly replacing earlier defined policy domains and vested interests.

24 James McQuade, "Improving the effectiveness of EU policy: the challenge of auditing the 2021-2027 MFF", in Brigid Laffan and Alfredo De Feo (eds.), *EU financing for the next decade. Beyond the MFF 2021–2027 and the Next Generation EU*, European Union Institute, 2020, p.92.

25 For a critical discussion on the use of GNI as basis for funding of the EU budget and related complications, see the special report of the European Court of Auditors, Special report 25/2022: Verification of Gross National Income for financing the EU budget. Risks in data compilation well covered overall, but scope for increased prioritisation of actions, 2022.

26 European Commission, "Commission staff working paper, The added value of the EU budget", 29 June 2011, p.2.

27 European Commission, 'The EU Budget Review, Communication from the Commission', COM(2010)700final, 2010.

Structure of the EU budget

EU expenditure for 2021-2027 totals €1,824.3 billion, made up of €1,074.3 billion for the MFF and €750 billion for the NGEU (at 2018 prices);[28] at 2022 prices: €2,017.8 (total), €1,210.9 (MFF), €806.9 (NGEU).
These amounts are for the maximum commitments.

Budget headings:
1. Single Market, Innovation and Digital
2. Cohesion, Resilience and Values
3. Natural Resources and Environment
4. Migration and Border Management
5. Security and Defence
6. Neighbourhood and the World
7. European Public Administration

The contours of the MFF are laid down in the Multiannual Financial Framework Regulation, which defines how much the EU can spend. The Own Resources Decision defines where EU revenues come from. The negotiations take place on the basis of the Commission's proposals for the MFF and the resources.

The Council decides by unanimity on the MFF and own resources. The European Parliament has the right to approve or reject the decision by the Council on the MFF (relevant for the discussion below of making the EU budget more 'European'). The European Parliament gives its opinion on the own resources.[29] Each member state ratifies the own resources decision. A mid-term review of the MFF has been dropped (although the European Commission still intends to conduct one). [30]

28 European Commission, Headings (europa.eu), accessed 21 January 2023; Council of the European Union, COUNCIL REGULATION (EU, Euratom) 2020/2093 , 17 December 2020.

29 European Council and Council of the European Union, Policies, accessed 15 December 2022.

30 European Commission, "State of the Union – Letter of Intent", 14 September, 2022.

The financing of the MFF is laid down in the *Own Resources Decision*. The own resources ceiling for the current MFF is now set at 1.46% of GNI for commitments and 1.40% of GNI for actual payments.[31] In addition, to finance the NGEU, the own resources ceiling was 'exceptionally and temporarily' raised by 0.06% of the EU's GNI on top of the proposed permanent increase from 1.2% to 1.4% of GNI.[32]

2.2 Decision making and negotiations

Negotiations for a new MFF usually start halfway through the budget period. The Commission presents assessments of ongoing expenditures and drafts the proposal for the next MFF via a package that includes the MFF Regulation and the Own Resources Decision.[33] Subsequent negotiations between member states are usually lengthy, complex and conflictual.[34] Different from what was initially expected (or hoped), national positions barely changed when net receivers became net contributors because national and regional vested interests also make it difficult for a government to take a more reformed stance in the budget negotiations.

The German Institute for International and Security Affairs distinguished three different blocks in the negotiations for the MFF 2021-2027: the 'status quo preservers', the 'moderate modernisers' and the 'rigid savers'.[35] The group of status quo preservers comprised of (former) net recipient countries from southern and central-eastern Europe spoke out against cuts in structural and agricultural funds and advocated for a significant increase in the budget. The moderate modernisers (Germany, France, Belgium, Luxembourg, Finland and Ireland) generally advocated for modernisation of traditional spending policies and own resources, without necessarily opposing increased contributions. The rigid savers consisted of Sweden, Denmark, Austria and the Netherlands. This group argued

31 European Council and Council of the European Union, Long-term EU budget 2021-2027 and recovery package - Consilium (europa.eu), accessed 21 January 2023.

32 European Parliament, The Union's revenue | Fact Sheets on the European Union | European Parliament (europa.eu), accessed 21 January 2023.

33 European Council, "Negotiating the EU long-term budget", 8 November 2022.

34 Peter Becker, "A New Budget for the EU Negotiations on the Multiannual Financial Framework 2021–2027", SWP Research Paper, August 2019, p.5.

35 Peter Becker, "A New Budget for the EU Negotiations on the Multiannual Financial Framework 2021–2027".

for bigger cuts in Common Agricultural Policy (CAP) and structural funds so that newer policies could be financed and the budget could be limited to 1% of EU gross national income.[36]

The Dutch position

As happened in earlier MFF negotiations, the Netherlands advocated in a position paper in 2018[37] for a significant reprioritisation in EU funding, focusing on policy areas with, arguably, the most European added value, such as innovation and research, and migration and border control. The Dutch government indicated that it could not accept an increase in gross national contributions, which, accordingly, would further exacerbate its position as one of the relatively largest net contributors. Moreover, it expressed its caution regarding the introduction of new forms of own resources, indicating that it would evaluate any proposals against the need for simplicity, transparency and the safeguarding of national competencies. In addition, it advocated greater conditionality of EU funding in the fields of structural reforms, rule of law and migration, and also called for greater flexibility. The emphasis on conditionality has played an important role in the acceptance of the Recovery and Resilience Facility.

As regards own resources, the Netherlands has traditionally been cautious of new forms of own resources. However, the Dutch government is, in principle, open to the adoption of the proposed new own resources.[38] It has indeed judged that the adoption of a revenue system based on the emissions trading system (ETS), for instance, could be financially profitable to the Netherlands. However, it has expressed concerns over the stability and dependability of the proposed new streams of revenue, as well as the potential implementation burden. Moreover, for the Netherlands, it remains important that any new own resources are charged at national level, not at EU level.

36 Ibid.

37 Government of the Netherlands, "Dutch position paper on new MFF", February 2018.

38 Tweede Kamer der Staten-Generaal, "22 112 Nieuwe Commissievoorstellen en initiatieven van de lidstaten van de Europese Unie - Nr. 3279, Brief van de Minister van Buitenlandse Zaken", 28 January 2022.

2.3 Modifications in the MFF 2021-2027

Negotiations over the current MFF took place against the backdrop of the UK withdrawing from the EU, a number of major cross-border challenges such as climate change, the digital transformation, the migration and refugee flows, and – at the final stage – the Covid-19 pandemic.[39] In May 2018 the Commission tabled its MFF package, which, in a substantial re-allocation of expenditures to policies with alleged EU added value, foresaw a reform of the CAP, the abolition of rebates and the introduction of new own resources.[40] The proposal, however, was significantly watered down in the ensuing negotiations between member states and between Council and European Parliament. To the disappointment of the 'modernisers', the agreed package included only moderate cuts to agricultural funds (from 36% to 31%) and cohesion spending (from 34% to 31%), while leaving less scope for other and 'newer' policy priorities.[41]

The 2021-2027 budget nevertheless included some important novelties. Although largely incomparable due to Brexit and the integration of the European Development Fund in the new MFF, the 2021-2027 framework introduced a substantial increase in the overall budget as compared to the previous one, as the €1,074.3 billion MFF (€960 billion for the previous period) was complemented with a €750 billion extraordinary recovery instrument, NGEU (2018 prices).[42] To finance the latter instrument, member states agreed on the issuance of common debt, thereby breaking the important taboo of debt financing. Despite only moderate cuts in traditional MFF spending, 'new priorities' gained some ground. The new priorities, however, made up the biggest share of the NGEU, in which great emphasis is placed on the green and digital transitions.[43]

Furthermore, the package included the agreement on the new *plastic own resource* and paved the way for the Commission to come up with additional sources of revenue to cover NGEU debts. Following this agreement,

39 European Commission, "The evolving nature of the EU budget", *EU budget policy brief*, October 2021, p.10.

40 Alfredo de Feo, "The Multiannual Financial Framework 2021-2027: Ambition or Continuity?", in Brigid Laffan and Alfredo De Feo (eds.), *EU financing for the next decade. Beyond the MFF 2021–2027 and the Next Generation EU, European Union Institute*, 2020, p.7.

41 Margit Schratzenstaller, "Raising the resources to open the European sluice-gates", *Social Europe*, 30 November 2021.

42 European Council and Council of the European Union, EU budget, accessed 17 January 2023.

43 Ibid.

the Commission put forward three new sources of revenue: the first based on revenues from the emissions trading system (ETS), the second on revenues from the EU carbon border adjustment mechanism (CBAM), and the third on a levy on the world's largest multinationals.[44] It should be noted, however, that there are many obstacles towards the adoption of these three new sources of revenue and the new own resources might not only be used to finance the RRF. Moreover, even if adopted, the new revenue sources would far from cover the money borrowed for NGEU.[45] The repayment is therefore likely to play a role in negotiations over the next MFF. Formally, the agreement on the RRF only states that a start on the payback must be made. No ambitions for repayment are formulated. This makes it reasonable to expect that repayment is, in essence, pushed to later MFFs because an agreement on anything more than marginal repayments out of the next MFF will complicate a compromise, as it will take a cut from the available means. It is important, however, to resolve the question of how NGEU debts will be paid back – whether through a package of new own resources, budget cuts, additional national contributions, or some combination. If member states do not reach an agreement, the credit rating of the EU may suffer, resulting in higher borrowing costs.

Finally, the EU increasingly ties funding to conditionality in order to achieve important EU policy objectives – for instance in economic governance, rule of law and green transition.[46] To receive funds from the RRF, member states submit their reform and investment plans to the Commission and must specifically address issues flagged in the country-specific recommendations in the European Semester, as well as greening and digitalisation. Funding from the resilience fund is dependent on the extent to which these conditions are met.[47] Hence, conditionality is also a tool for redirecting the focus on to common goals.[48] Of course, as argued in the next section, an effective conditionality approach relies on the careful monitoring and evaluation of EU spending programmes.

44 European Commission, "The Commission proposes the next generation of EU own resources", 22 December 2021.

45 Simon van Dorpe, "Nederland dreigt hoge rekening te krijgen voor Europees coronaherstelfonds", *Follow the Money*, 3 November 2022.

46 Viorica Vita, "The Reinforced Conditionality Approach of the 2021-27 MFF", in Brigid Laffan and Alfredo De Feo (eds.), *EU financing for the next decade. Beyond the MFF 2021–2027 and the Next Generation EU*, European Union Institute, 2020, p.101.

47 European Commission, Recovery and Resilience Facility (europa.eu), accessed 17 January 2023.

48 Peter Becker, "Budgeting as the political creation of added value", *ECA Journal*, 2020, nr.3, p.37

3 Flexibility considerations in the run-up to the next MFF

Further reform considerations demand insight into proven added value. This opens the discussion on how well the current roles of the Commission and the European Court of Auditors (possibly with its network of independent national courts of auditors) are adapted to the expectations of effectiveness of spending, flexibility and conditionality requirements. This chapter outlines the contours of some of the relevant debates and concludes with a suggestion for case studies on the performance assessments of EU spending.

While focusing on flexibility, it is not the intention of this report to provoke too many thorny discussions on the size and composition. While there is little political appetite for any reforms in EU finances that would require Treaty change, there are a couple of reforms and innovations that could be explored in the lead-up to the next MFF negotiations. These reforms could potentially help maximise the performance of the MFF, make it more flexible and improve its financial sustainability. These options, as well as some more ambitious ones, are explored below – as they offer background for the discussion on the use of effectiveness audits. To guide future discussions on these topics, the points for discussion are listed in boxes.

3.1 Increasing flexibility

Arguably, any state budget suffers from inflexibilities. Budgets are not neutral, as there are many interests involved. As new governments are expected to define their medium-term budget plans, the contours of the budget, defining spending targets and priorities for the length of the period in office create inflexibility, particularly when a coalition government has to operate on the basis of hard-fought compromises. Adapting budgets is one of the key processes in democracies and it demands considerable political effort in finding agreements and skills in terms of budgeting techniques.

Lack of flexibility in the MFF relates, first, to the 7-year cycle.[49] This has been a cause of great controversy and has triggered reform proposals such as linking the budget cycle to the 5-year election cycle or to long-term Commission priorities.[50] As remarked by ECA in its annual report of 2014, 'The MFF periods have never been in line with the EU's strategy periods (2000-2010 and 2010-2020). This made it more difficult for the Commission to monitor and report on the contribution of the EU budget to the EU's overall strategy for the 2007-2013 MFF period.'[51] Second, once the overall budget is agreed, each of the approximately 40 programmes under the MFF needs a Regulation detailing objectives and ways of working.

Nevertheless, along the way, the MFF gained in flexibility to make adjustments in expenditures as well as in terms of income. First of all, the Flexibility Instrument (FI) and the Single Margin Instrument (SMI) were adjusted to allow for the financing of specific unforeseen expenditures.[52] Moreover, additional thematic instruments were introduced: the Brexit Adjustment Reserve of €5 billion, introduced in 2020 to support member states and economic sectors hit by Brexit; the European Globalisation Adjustment Fund of €1.3 billion, introduced in 2007 to support employees who lose their jobs in restructuring events linked to globalisation; and the Solidarity and Emergency Aid Reserve of €1.2 billion, introduced in the 2021-2027 MFF as a result of the merging of the European Union Solidarity Fund and the Emergency Aid Reserve to support member states and accession countries in the face of major disasters and for rapid responses to specific emergency needs within the EU or in third countries.[53] However, the amount reserved for these funds was reduced from the proposed €38 billion to €16 billion. It is also possible to reassign funds under the headings where programme budgets are not fully absorbed. Finally, more use is now made of back-to-back loans (loans for loans as, for example, used to support the Ukraine government) which allow for spending outside the constraints of the EU budget.

49 Jorge Núñez Ferrer, "Briefing paper options to address unforeseen events", p.3.

50 For a critical discussion on the 7-year cycle in the European Parliament, see European Parliament, Texts adopted - Interim report on the Multiannual Financial Framework 2021-2027 – Parliament's position with a view to an agreement - Wednesday, 14 November 2018 (europa.eu).

51 European Court of Auditors, Annual Report, 10 November 2015.

52 Replacing three previously separate instruments: the Global Margin for Commitments, the Global Margin for Payments, and the Contingency Margin. See: European Commission, "Flexibility and special instruments";

53 Special European Council, 17-21 July 2020; European Commission, "Flexibility and special instruments"; European Council, "Long-term EU budget 2021-2027 and recovery package".

The loan-based NGEU is based on the difference between the ceiling of the own resources and the ceiling of the MFF (the 'headroom'). Apart from the flexibility this margin offers, the headroom guarantees the triple-A states for the loans issued by the Commission.[54]

Sunset clauses

A way to further enhance flexibility would be to strengthen the use of 'sunset clauses' in EU programmes. When tied to close reviews, such clauses prevent payments from becoming redistributive entitlements and make way for other programmes should funds no longer be effective in meeting EU objectives. The current decision-making procedure is in itself a general sunset clause, as priorities and programmes are renegotiated every seven years. However, more explicit forms of sunset clauses in programmes might bounce against vested interests. Yet, a sunset clause tied to programmes, linked to an effectiveness assessment in cases of prolongation, could help to underline the fact that regular revision of priorities is the rule rather than an exception. A sunset clause will not affect flexibility for the length of a programme, but at least it offers the opportunity for a structured review at the end of a programme (varying from shorter programmes of say three years to longer-term programmes of, for example, ten years). Although the duration of the multiannual framework is fixed, programmes within the budget will offer possibilities for more substantive reconsiderations (compare the multitude of programmes and deadlines in national budgets).

Sunset clauses and effectiveness assessments can replace earlier attempts to have a mid-term review procedure. The 2014-2020 MFF package included a compulsory mid-term review of the functioning of the MFF. Such a review 'can improve flexibility by providing an opportunity to redefine EU spending priorities and introduce changes necessary for a smooth and more realistic implementation of the MFF in the second part of the term'.[55] Although the mid-term review was modest in scope due to practical difficulties – as mentioned above – but also due to 'legal restrictions, the unwillingness of various member states to modify fixed ceilings and its misalignment with the EU institutions'

54 European Commission, "The 2021-2027 EU budget – What's new?", accessed 17 January 2023.

55 Magdalena Sapala, "Strengths and Weaknesses of the EU Budget Flexibility 'toolbox'", in Brigid Laffan and Alfredo De Feo (eds.), *EU financing for the next decade. Beyond the MFF 2021–2027 and the Next Generation EU, European Union Institute*, 2020, p.259.

political calendar',[56] it did result in the reinforcement of some of the special instruments introduced. Although the European Commission intends to conduct a mid-term review, its role in the 2021-2027 MFF has been downgraded. Sunset clauses might be an alternative to such full-blown and close-to-impossible mid-term MFF reviews.

Duration of the MFF

Another proposal that has been floated to enhance the MFF's flexibility, is to change its duration. As mentioned, with the introduction of multiannual budgeting, the EU budget lost an important degree of flexibility. Although a return to a purely annual budget may be neither realistic nor desirable, any shortening of the MFF's duration could potentially improve the EU's ability to respond to changing priorities. We will refrain here from more in-depth discussion on aligning the MFF to the EU's political cycle, as this would change the interinstitutional balance.

Questions for discussion
- Could explicit sunset clauses combined with effectiveness assessments contribute to the flexibility of the MFF?
- Could sunset clauses leave the 7/5-year cycle as it is and offer opportunities for more dynamic programming?

Make money scarce: GNI-based funding

Attention to own resources is one way now being explored to address new challenges. However, more own resources in themselves do not address the question of how to reconsider flexibility within the agreed budget. A discussion on a fixed percentage of GNI might help to recommit to the scarcity principle in budgets.

One of the novelties in the 2021-2027 MFF package was the introduction of a new source of revenue and an agreement to explore additional sources to cover NGEU debts.[57] However, even if adopted, these would not yet be sufficient for

56 Eulalia Rubio, "The next Multiannual Financial Framework (MFF) and its flexibility", 2017, p.13.

57 For discussions on the revenue collection in relation to GNI, see European Court of Auditors, 'Verification of Gross National Income for financing the EU budget', 2022; European Court of Auditors, 'The EU's financial landscape', 2023.

repayment of NGEU debts.[58] The Commission is therefore set to propose new own resources which could include a financial transaction tax and an own resource linked to the corporate sector.[59] This new generation of own resources faces considerable obstacles, not in the least because of the required unanimity. Some member states, for example Sweden and Germany, are generally rather sceptical about new EU levies. Others, such as Poland, are concerned that they would bear a disproportional cost.[60]

Irrespective of the type of revenue source, member states tend to focus on their own net balances. Own resources add to the problem of *juste retour* by also linking *juste retour* to revenues. Member states will meticulously assess what an own resource will cost them. Although the MFF's heavy reliance on GNI-based contributions may not be ideal, the GNI-basis does offer the fairest (i.e. richest member states carry the biggest weight), easiest and most transparent revenue base.

Under the GNI basis, NGEU debts could be covered through (redistribution of) the existing budget or through a – temporary – higher percentage of GNI. It remains important, however, to adequately resolve the question of how exactly NGEU debts are going to be repaid, as the current way of working may set a dangerous precedent of shifting costs into a distant future. Ignoring the precise payback in the setting up of new facilities might, however, be tempting. Moreover, as long as member states do not reach agreement, the credit rating of the EU could suffer, resulting in higher borrowing costs[61] and possibly also erode public support once questions over repayment can no longer be avoided.

To avoid the impression that the choice for a GNI-based MFF is an attempt to economise on the EU budget as well as to create a basis for negotiations, it might be a possibility to consider 1) a slightly higher GNI than the current MFF ceiling under the condition that the ceiling is a fixed maximum with the purpose of ensuring careful selection of priorities within the pre-agreed budget (possibly even through a limited Treaty change (Article 48(6) TEU)), and 2) the precondition

58 Simon van Dorpe, "Nederland dreigt hoge rekening te krijgen voor Europees coronaherstelfonds", *Follow the Money*, 3 November 2022.

59 European Parliament, "MEPs clear way for new sources of EU revenue", 23 November 2022.

60 Simon van Dorpe, "Nederland dreigt hoge rekening te krijgen voor Europees coronaherstelfonds", *Follow the Money*, 3 November 2022.

61 Ibid.

of effectiveness assessments of programmes tied to an agreement on an increase in GNI-based contributions.

Questions for discussion

- Could a GNI-based MFF be used to constrain the pressures to find additional finances outside the MFF and to stimulate reassessments of the existing priorities in the MFF?
- What is a realistic and acceptable maximum percentage for a GNI-based MFF?
- What reform package can be imagined when considering a discussion on the GNI-basis?
- How could repayment of new common debts be prevented from being pushed into the future?

3.2 Maximising European added value

Starting from scarcity

Economics is the science of scarcity. Its sub-discipline of public finances studies the behaviour of governments in making decisions on the distribution of scarce resources over the three main functions of public finance: allocation (public goods), macroeconomic stabilisation, and redistribution.[62] When scarcity is the starting point, political decision makers are incentivised to sharpen their decisions and to prioritise their ambitions based on assessments of the European added value of EU spending. This could lead to reassigning revenues in order to remain within the margins of the agreed budget. Although this is, in the end, a *political* decision, the consequence of the current inflexibility in the EU budget is that, when faced with new priorities or challenges, decision makers are forced to move outside the constraints of the existing budget and create new programmes and financial facilities.

Point for discussion

- Should scarcity be re-examined as a governance mechanism in the EU budget?

62 Musgrave, R. A. *The theory of public finance*, Tokyo: McGraw Hill Kogakusha, 1959.

Linking the financing of programmes to effectiveness assessments: the role of ECA

One way to strengthen the added value of the EU budget is to explore the role of performance assessments in decision making.[63] Given the host of issues related to performance, we can only touch on some of the most relevant dimensions and link the discussion in particular to the role, functioning and impact of the ECA as a basis for further analysis. The *how* of performance audits influences the visibility, quality and ownership of performance assessments.

Effectiveness studies are being carried out first of all by the Commission through its impact assessments and regular reviews.[64] In addition, the ECA divides its work between controlling the legitimacy of spending (its external independent audit role) and dedicated effectiveness studies published as Special Reports. Moreover, at national level the emphasis in the work of dedicated audit bodies lies essentially on controlling the *legitimacy* of EU spending (accountancy). National audit offices barely play a role in assessing the *effectiveness* of EU programmes in their member states[65] and national courts of auditors seem to cherish their independence (read: distance) from EU programmes.[66]

Further analysis is required of the effectiveness of programmes under the MFF – and some questions for debate can be identified. The first question concerns the feasibility of effectiveness assessments in current MFF decision making. The time required for moving from programme initiation and tendering of projects in the first years of the MFF, combined with the number of years for implementation of programmes and projects, leaves little room for mid-term assessments.[67] The second question concerns the role of the Commission,

63 Eulalia Rubio, "European added value: what does it mean?", *ECA Journal*, 2020, nr.3, p.144.

64 European Commission, How decisions are being made, How decisions are made (europa.eu). Accessed 16 February 2023.

65 But for The Netherlands, see the rather exceptional report: Algemene Rekenkamer, *Toegevoegde waarde EU-subsidies in Nederland*, Den Haag, 2022.

66 It is important to note that national audit offices are strictly independent from the executive at any level.
Article 287(3) includes TFEU in the functioning of ECA, Article 287(3): 'The Court of Auditors and the national audit bodies of the Member States shall cooperate in a spirit of trust while maintaining their independence. These bodies or departments shall inform the Court of Auditors whether they intend to take part in the audit.' Legal Framework | EUROPEAN COURT OF AUDITORS (europa.eu)

67 See, for example European Court of Auditor, Annual report on the performance of the EU budget (ECA 2020), ibid, especially paragraph 1.10 and figure 1.2.

which is the manager of the EU budget as well as the assessments. A third question is whether the legitimacy of EU spending in the eyes of the wider public is best served with the current ways of working regarding communication on EU added value. Is the current information sufficient, timely and independent (including being visible through national bodies close to programmes in the member states and in national media)? Fourth, a discussion seems to be in place on the roles and functioning of the ECA and the involvement of national courts of audit. Apart from the ECA's rather centralised ways of working, and the problematic role of its national counterparts, NGEU has added to the workload and the complexity of eligibility criteria for dispatching and assessing RRF projects.[68]

A study of the Bertelsmann Stiftung suggests that, for well-defined policy fields, added value quantifications in the EU could be improved.[69] Of course, such evaluations would have to rely on (economic) definitions of research themes aimed at strengthening political decision making and transparency.[70] As to independent and systematic assessments, this demands posing questions regarding the roles and budgets of the ECA. Moreover, and even more sensitive, this will demand that national courts of audit are willing to be closely involved, which raises questions as to their having sufficient capacity and respecting the principle of subsidiarity. Ideally, steps towards systematic performance audits would be considered together with a move towards a more unitary budget – also via including some of the instruments that fall outside of the EU budget so that they are subject to the same level of auditing standards.[71]

68 European Court of Auditors, Annual report 2020., 2021. See also the relevant Motions in Dutch parliament referred to above.

69 Bertelsmann Stiftung, "The European Added Value of EU Spending: Can the EU Help its Member States to Save Money?", 2013, p.8.

70 Eulalia Rubi, "The "added value" in EU budgetary debates: one concept, four meanings", Notre Europe, 2011, p.6.

71 James McQuade, "Improving the Effectiveness of EU Policy: the Challenge of Auditing the 2021-2027 MFF", in Brigid Laffan and Alfredo De Feo (eds.), *EU financing for the next decade. Beyond the MFF 2021–2027 and the Next Generation EU*, European Union Institute, 2020, p.92.

Questions for discussion

- Which European and national institutions are involved in effectiveness studies? Are these bodies independent from policy making and do they have a recognised independent position?
- To what extent are performance audits of EU programmes assessed, and to what extent are conclusions incorporated into the redesign of the EU budget?
- Are decisions on continuation of programmes based on performance assessments?
- Is it possible to involve national audit offices – including streamlining and financing their involvement through the MFF?

Strengthening the European dimension by QMV?

As regards the political priorities in the MFF, a more fundamental reform option would involve introducing Qualified Majority Voting (QMV) in the Council (via the passerelle clause/Article 312.2 TFEU) and/or by extending the powers of the European Parliament through co-decision (requiring Treaty change). At the moment, any revision in MFF Regulation is subject to unanimity in the Council, which makes it difficult to move resources between different headings during the running period. Yet, the Interinstitutional Agreement of 17 May 2006 for the MFF 2007-2013 allowed for a limited revision of the MFF Regulation via QMV – which came to an end with the coming into force of the Lisbon Treaty. Hence, there is a precedent.[72] Introducing QMV into the adoption of the MFF Regulation (with the exception of the Own Resources) would make the process less prone to individual veto players and would arguably provide the European Commission with more room to manoeuvre for a tailored MFF proposal and for reshufflings during the implementation of the budget. In addition, QMV – including the voice of the European Parliament – would arguably offer a stronger emphasis on European (rather than national) priorities.[73] Evidently, such a move would affect the carefully crafted interinstitutional balance.

72 Stefan Lehner, “The Dual Nature of the EU Multiannual Financial Framework”, p.40.

73 Stefan Lehner, “The Dual Nature of the EU Multiannual Financial Framework”, pp.39-40; Friedrich Heinemann, “Strategies for a European EU Budget,” Working Paper for the Brussels Symposium, 14 January 2016.

Questions for discussion

- With a view to public support, if effectiveness assessments were available, could, as a next step, QMV and co-decision contribute to more flexibility in EU budget priorities?
- Would a compromise on a reform package be helped by extending QMV?

4 Concluding remarks: targeting effectiveness assessments

Many discussions are taking place on reforming the MFF and suggestions have been made for major overhauls of its finances and procedures. However, in reality, pragmatism and modesty are required when discussing feasible reforms. This report concludes that a logical start to prepare for a next round of MFF discussions would be to look at what we know about the performance of programmes and about the (multilevel) system for assessing the effectiveness of EU spending. Addressing flexibility – one of the main challenges – may have to start with explicitly bringing performance assessments into debate on the future of the EU budgets and its procedures. Decisions based on European added value and communication directed at the general public will, in part, depend on independent information regarding choices and added value.

Given the many questions surrounding the topic of effectiveness, additional analysis is required as to how European added value is currently assessed and used in decision making on the MFF. Given the range of reports available and the financial interests at stake, cohesion policy programmes seem to be a suitable area to examine performance assessments. Such an analysis could address the quality of the reports and the follow-up, and could also look into the involvement of various actors in the quality evaluations.

Questions for discussion

- How is effectiveness studied? By whom and through which structures?
- What reports have been made available regarding the effectiveness of programmes and what suggestions have been formulated? What impact have the assessments had?
- What conclusions result from the case studies on cohesion policy regarding the functioning of the (multilevel) system through which performance is assessed?[74]

74 Similarly, the rural development part of agriculture expenditure mirrors and complements the regional and urban policy, albeit for a minor part of the economy.