# Counterpoint

## The EU Budget and the CAP: An Agenda for the Review?

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In *EuroChoices* 5(1), Professor David Harvey offered a possible agenda for review of the EU budget in general and the Common Agricultural Policy (CAP) in particular. In this, unfortunately, we feel that he has dismissed rather too lightly factors that will both shape and limit the potential outcomes of the review. As a result we fear that his agenda, by ignoring the politics of EU budget-making, would risk total stalemate.

Professor Harvey appears to disregard the process by which any reform, presumably requiring agreement within the European Council, will be achieved. The starting point for any discussion about the EU budget is to recognise that its political significance far exceeds its monetary value. Furthermore, the budget reforms since 1988 have reinforced the balanced budget rule as the key instrument of financial discipline (Ackrill and Kay, 2006).

Unanimity voting creates an inter-governmental negotiating process. Getting 27 governments to agree will require compromise and trade-off, especially where financial (for which read political) sacrifices will be needed. With the EU budget consequently operating as a zero-sum game, the rational response of governments is to defend prevailing financial transfers. Indeed, the distribution of shares of budget contributions and receipts across member states has been extremely stable over time.

Note, for example, how the EU12 agreed a CAP reform in 1992 that left the distribution of CAP transfers largely unchanged, despite the extent of changes to support instruments. More recently, the EU15 imposed on ten applicants a financial agreement for enlargement that preserved their own budget transfers in the face of this largest ever expansion of the EU. Any reform agenda that fails to recognise the significance of this issue to the member states will not succeed.

So, what might a reform agenda look like that recognises these political realities? Given the nature of decision-making as outlined, it is inevitable that CAP reform will be incremental. However, recent historical institutionalist scholarship and long standing analyses of public finance both stress the often significant cumulative effects of incremental change.

When Professor Harvey described CAP spending as 'mandatory and 100 percent funded from the EU budget' (page 23), he forgot about spending on rural development. This offers a direction in which further change can move. Furthermore, the 1999 reform also introduced modulation, a change that was developed in 2003 and which can be taken further. So, let us start by proposing an increase in the share of CAP spending for Pillar II measures, by increasing the percentage of total Pillar I direct payments (Single Farm Payment (SFP) plus unconverted post-1992 payments) that must compulsorily be modulated. This would also address a problem with the SFPs that Professor Harvey points out, that even these decoupled Pillar I payments are not very effective at delivering desired environmental and sustainable rural outcomes.

Let us go further, by requiring all post-1992 payments to be converted to SFPs. Along with greater Pillar II funding member states can, where necessary, target the expanded Pillar II resource-base at regions where they fear the removal of the post-1992 payments could cause localised difficulties.

Modulation is now compulsory, but this simply transfers EU funds from Pillar I to Pillar II, *on top of which* is then added national co-financing. As a result, EU spending is left unaltered but even more resources in total are directed to the CAP. So, let only x per cent of the EU money taken from the direct payments be recycled into Pillar II (where x can be negotiated, but the opening proposal should be high, say 75 per cent). The balance of funds can then come through the national co-financing channel already in place. Whether total EU plus national spending remains equal to pre-reform EU spending, or whether the post-reform EU plus national total is less, propose the latter then let the member states negotiate.

A limit on the total payment individual farmers can receive is already back on the agenda. If this raises hackles, an alternative is to require a larger cut in direct payments from the largest farmers, say double the standard modulation rate as an opening proposal. They may be able to maintain or even increase total CAP receipts if they can claim sufficient funds through rural development measures, but if they are capable of delivering the desired environmental and or rural policy goals efficiently, then no problem.

Repeating another aspect of the 2003 reform, to garner member states' support, ensure funds recycled from Pillar I into Pillar II remain within the member state to which they were initially allocated. But, if some countries wanted to promote rural development measures even more than the enhanced modulation would provide for then, again as with 2003, let them do so. This time, however, have no upper limit on the amount of direct payments that can voluntarily be modulated.

As a result of all this, EU spending on the CAP will fall. Total EU plus national spending on the CAP may fall or remain unchanged, but the proposal should seek an overall cut (there must be wiggle-room built in for compromise and trade-offs if 27 countries are to agree). Less money would go to Pillar I measures, with more resources going directly to those measures that are most effective at delivering the wider policy goals desired of and achievable by rural communities.

There is nothing radically different here, but it keeps nudging the CAP, incrementally, in a better direction, whilst leaving the door open for further developments in future. But what is the ultimate goal? These proposals, as well as being consistent with prevailing constraints on decision-making and potential reform options, will also take the CAP in a direction consistent with the CARPE proposal from Professor Buckwell.

As for the UK rebate, Professor Harvey repeats one of the great red herrings of our time. The UK does not get a rebate because of the CAP. What the CAP did was create a situation where some countries were significant net contributors to the EU budget. The UK got a rebate because its net contribution was deemed too far out of line with its relative income per capita. At no point did Germany get a rebate, despite the CAP creating for it even larger net contributions than the UK. The subsequent abatement on its contribution to the UK rebate was made in recognition of its overall contribution to the EU budget.

Thus, since the UK got rebates from 1980 because of its relative poverty, its relative wealth today renders arguments for a continued rebate redundant. Should the rebate just go? In economic terms, absolutely. In political terms, however, there is a clear argument for retaining it a little longer: to use as a bargaining chip against those countries who receive significant 'rebates' on the cost of their agricultural sectors (Peet, 2005).

Such a trade-off was hinted at by the UK in the latter part of 2005. Given the time-constraint on the overall negotiations and impossibility of agreeing a matching CAP reform within that timeframe, such a goal was unachievable. In the context of the forthcoming review, however, the rebate may still have sufficient weight as a bargaining chip to use within less time-constrained talks on CAP reform. In this context, abolition of the rebate might even be easier to sell at home than the reduction agreed in 2005 (except, possibly, to those largest of UK farmers who may lose out on some of their erstwhile payments received simply for being big).

## Further Reading

Ackrill, R. W. and Kay, A. (2006). Historical Institutionalist Perspectives on the Development of the EU Budget System. *Journal of European Public Policy*, 13(1), 113-133.

Peet, J. (2005) *The EU Budget: a way forward*. Centre for European Reform Policy Brief: http://www.cer.org.uk/pdf/policybrief_peet_budget_july05.pdf

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## Summary

Professor David Harvey's proposed agenda for CAP reform in *EuroChoices* 5(1) is, we believe, unrealistic. It pays insufficient attention to the politics of EU policy-making and ignores the importance countries place on protecting their shares of EU spending. We recognise the incremental nature of CAP reform, but believe this can lead to significant cumulative effects. Our proposal builds on modulation to transfer more CAP spending from Pillar I to Pillar II. Farmers receiving the largest payments should have their payments cut through higher compulsory modulation rates. We also seek a reduction of EU spending on the CAP, with greater national contributions achieved through the established channel of co-financing.

## Pullquote

David Harvey's proposed agenda for CAP reform is unrealistic. It pays insufficient attention to the politics of EU policy-making and ignores the importance countries place on protecting their shares of EU spending.