CHAPTER 9

The Budget

Who Gets What, When, and How?

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Summary

The budget is a focus for repeated negotiation among the European Union (EU) member states and institutions, following firmly established rules. In 1988, the EU moved—after several years of bruising annual negotiations—to multiannual 'financial perspectives', or package deals, for which the Commission makes proposals and the 'Budgetary Authority'—the Council, particularly the European Council, and the European Parliament (EP)—negotiates agreement. This institutional change that was later constitutionalized by the Treaty of Lisbon has concentrated budgetary politics into periodic strategic bargains that link national costs and benefits, reforms of the common agricultural policy (CAP), regional imbalances, future-oriented policies, and enlargements. This pattern was reinforced by subsequent budget packages in 1992 (Delors-2), in 1999 (Agenda 2000), in 2006 (the financial perspective for 2007–2013), and in 2013 (the Multiannual Financial Framework for 2014–2020). Over these years, the structure of the budget changed only slightly; agricultural and regional expenditure remain the two large spending blocks. The outbreak of Covid-19 coincided with the regular adoption of a new Multiannual Financial Framework (MFF) (2021–2027) and led to a significant innovation: after intense discussions, mainly between net contributors and net beneficiaries, the European Council in July 2020 found a political agreement not only on the new MFF—which by and large stayed within the distributive pattern of the previous one—but also on a sizeable package of an additional temporary recovery fund (mainly directed towards member states in the form of grants and loans) financed for the first time by large-scale borrowing on the capital markets by the Union.

Introduction

Historically, budgets have been of immense importance in the evolution of the modern state and they remain fundamental to contemporary government.[1] This chapter enters the labyrinth of EU budgetary procedures in an attempt to unravel the characteristics of budgetary politics and policy-making. Where EU money comes from, how it is spent, and the processes by which it is distributed are the subjects of intense political bargaining. Budgets matter politically, because money represents the commitment of resources to the provision of public goods and involves political choices across sectors and regions.

The politics of making and managing budgets has had considerable salience in the evolution of the EU because budgets involve both allocative and redistributive politics (see Chapter 3). Typical distributive (or allocative) expenditure is that spent on research, trans-European networks, and the environment, while cohesion policy and agriculture are examples of redistributive spending. The significance and challenges of budgetary politics are accentuated in difficult economic times. The euro area crisis with its attendant policy prescription of budgetary cutbacks and fiscal consolidation further politicized budgetary politics, including the politics of the EU budget. Turmoil in Europe's southern neighbourhood has increased pressures for the provision of adequate budgetary resources to manage migration and Europe's external borders. With Brexit, the EU has lost a big member state that paid more in to the EU budget than it has received, thus leaving a gap. The ongoing retrenchment in United States foreign policy and related calls for a stronger role of Europe in the burden-sharing of security costs have fuelled discussions on the higher provision of resources devoted to European defence. Most prominently, the Covid-19 pandemic and the high financial needs to support the recovery brought the EU budget to centre stage with intensive debates on burden-sharing but also a remarkable readiness to find innovative solutions for a sizeable common fiscal response.

Budgetary issues have inevitably become entangled with debates about the nature of the EU, the competences of individual EU institutions, and the balance between the European and the national levels of governance. Budgetary flows to the member states are highly visible so that 'winners' and 'losers' can be calculated with relative ease. As a result, budgetary politics are more likely to become embroiled in national politics and national electoral competition than is rule-making.

Questions about the purpose of the budget and the principles that govern the use of public finance in the Union are linked to wider questions about the nature international organization. In that context, the budget is also a useful yardstick with which to measure a type of integration that differs from the creation of a single market and the harmonization of rules and regulations (see Chapter 5). This utility was evident in the 2017 White Paper on the Future of Europe, in which the Commission offered five scenarios on the potential state of the Union by 2025 depending on the choices Europe will make. Each scenario (carry on, nothing but the single market, those who want more do more, doing less more efficiently, doing much more together) implied changes in the budget's size and composition (Commission 2017g). The size and scope of the EU budget also have implications for the operation of a vast range of policies. Moreover, a growing body of literature finds that EU budgetary decisions and management affect support for European integration (Chalmers and Dellmuth 2015; Dellmuth *et al.* 2016, 2018; Gross and Debus 2017; Schraff 2013, 2017).

The existence of the EU budget has often been justified and explained by its different functions: (a) as a means of side-payments to specific states or groups that are necessary to gain the overall consensus and political cement on further economic, particularly market, integration; (b) as the source for financing European public goods that benefit not only individual member states but also European citizens at large; (c) as the basis for redistribution[2] from richer to poorer parts of the Union which—following the value of European solidarity—fosters economic convergence towards a higher standard of living across the EU; and (d), in particular since the Covid-19 pandemic, as an insurance mechanism that allows for a temporary common response to a shock .

The process of managing, rather than just formulating, budgets raises questions about the management capacity of the Commission, but also about that of national authorities. All EU institutions and bodies, in particular the European Court of Auditors, are paying increasing attention to the impact of fraud on the budget and searching for better ways to protect the financial interests of the EU.

A thumbnail sketch of the budget

In the early years of the Union, the budget was a financial instrument similar to those found in traditional international organizations. The budget treaties of 1970 and 1975 led to a fundamental change. These treaties established the constitutional framework for the finances of the Union in a number of important respects. They created a system of 'own resources' which gave the EU an autonomous source of revenue, consisting of three elements: customs duties; agricultural levies; and a proportion of the base used for assessing value-added tax (VAT) in the member states, up to a ceiling of 1%. The 1970 agreement on own resources was subsequently altered several times. One basic principle was that this revenue base should apply to all member states, regardless of their size, their wealth, the pattern of EU expenditure, or their ability to pay. This was to cause increasing difficulty in the years to come.

The 1970 and 1975 Budgetary Treaties also altered the institutional framework for reaching decisions on the budget. The European Parliament (EP) was granted significant budgetary powers, including the rights to increase, reduce, or redistribute

expenditure in areas classified as 'non-compulsory' expenditure (essentially not agricultural spending, which was classified as 'compulsory'); to adopt or reject the budget; and to give annual discharge, through a vote of approval, to the Commission for its implementation of the budget. The 'power of the purse' gave the EP leverage in its institutional battles with the Council of Ministers and allowed it to promote its autonomous policy preferences. The 1975 Budgetary Treaty also provided for the creation of the independent Court of Auditors to enhance accountability in the budgetary process. The Treaty of Lisbon (ToL) constitutionalized the informal practices in EU budgetary decision-making that had emerged since the 1980s (including the key role of the multiannual budget plans) and aligned the annual process with the role of the Council and EP in the 'ordinary legislative procedure' (see Chapter 4).

A significant feature of EU budgets is the distinction between commitments and payments; the commitments budget is always larger than the payments budget (Box 9.1). Contrary to national budgets, the EU budget has basically not been debt financed until the Union's fiscal response to the Covid-19 pandemic.

After 1970, the emergence of the budget as a real instrument of European public policy was constrained by a basic factor that still shapes EU finances. The EU budget was, and remains, small in relation to Union gross national income (GNI), and to the level of public expenditure in the member states. In 2019, EU spending amounted to around €165.8 billion, which represented around 1% of EU GNI and was thus much less than domestic budgets, which collectively represent between 30 and 40% of European GNI.

Although the budget has little macroeconomic significance for the Union as a whole, it is very important for those member states that receive extensive transfers from the structural funds. For example, net receipts from the EU budget amounted in 2017 to 3.14% of GNI for Lithuania, 2.92% for Bulgaria, and 2.66% for Hungary. Moreover, its leverage effect and its capacity to mobilize resources are significant (De Feo and Laffan 2017). When considering co-financing obligations for member states, the mobilized funds have been estimated at roughly double the nominal

BOX 9.1 Appropriations

- **commitments:** legal pledges to provide finance, provided that certain conditions are fulfilled
- **payments:** cash or bank transfers to the beneficiaries
- **differentiated appropriations:** appropriations for commitments and payments often differ because multiannual programmes and projects are usually committed in the year they are decided and are paid over the years as the implementation of the programme and project progresses. Thus, if the EU budget increases, due for example to enlargement, commitments will increase before payments do. Not all projects and programmes are concluded, and appropriations for payments are therefore lower than for commitments.
- **non-differentiated appropriations:** relevant for administrative expenditure, agricultural market support, and direct payments

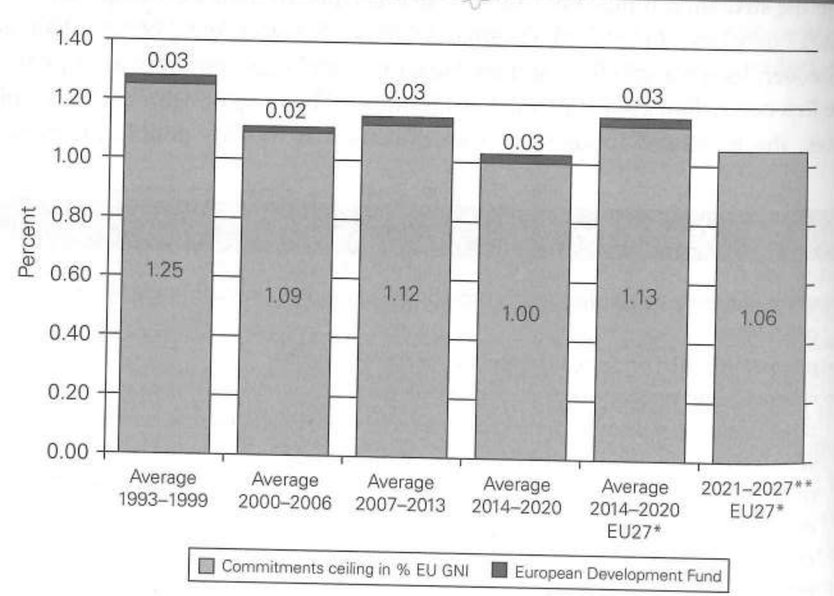
Source: Commission (2013a)

EU budget (Núñez Ferrer and Katarivas 2014). European Union spending programmes also mobilize constituencies within the member states, such as farmers (see Chapter 8) and regional groups (see Chapter 10), which have a material interest in the maintenance of their receipts.

The small overall size of the budget masked impressive increases in financial resources in the Delors-1 (1988–92) and Delors-2 (1993–99) budgetary agreements. The Berlin Agreement (1999–2006) and the Brussels Agreement (2007–13) included smaller increases. The agreement on the 2014–20 financial perspective represented a decrease in the EU budget as a share of EU GNI when including the UK expenditure; the 2021–2027 MFF proposal, agreed by the European Council in July 2020, envisaged (again) a decrease when comparing the EU27 averages (see Figure 9.1). This is, however, coupled with a temporary package of an extra €750 billion (in loans and grants) financed by borrowing on the capital markets (called 'Next Generation EU'), an increase in the own resource ceiling (on a structural basis to 1.4% of GNI and temporally for the purpose of borrowing by an additional 0.6%), and a commitment to introduce a new own resource based on non-recycled plastic waste and to further discussions on additional new own resources.

Despite the recent decision to borrow temporarily for the Union a significant sum for financing the recovery, the slenderness of EU budgetary resources highlights an important feature of the emerging European polity, namely the significance

FIGURE 9.1 The size of the EU budget as a percentage of gross national income (GNI)



*2014-2020 estimated commitments (UK expenditure excluded) in % EU27 GNI
** Own calculation based on European Council conclusions. The figure does not include Next Generation EU (see figure 9.5). European Development Fund integrated ("budgetized")

Source: (mainly) European Commission 2018 (https://ec.europa.eu/commission/sites/beta-political/files/euco-budget-booklet-june2018_en.pdf)

of regulation as the main instrument of public power (see Chapter 5), and it reflected a view that limited the role of public finance in European integration. This view was not always dominant. In the 1970s, the acquisition of sizeable financial resources for the budget was widely seen as essential to integration. In particular, it was anticipated that in the run-up to economic and monetary union (EMU) (see Chapter 7), a larger budget would be necessary to deal with external shocks and fiscal stabilization, which member governments would no longer be able to deal with through management of their own currencies. The view that there could be strong Union government focused on liberalizing and opening up national markets, with limited financial resources, gained ground in the 1980s, as Keynesian economic policies, which emphasized an interventionist role for the state, were discredited in favour of monetarist approaches, which stressed the efficiency of free markets and the benefits of price stability. The capture of the EU budget by agricultural interests in the 1970s made it difficult for arguments in favour of a stronger distributive role for the European centre to win political ground (see Chapter 8). The European sovereign debt crisis placed the question of the Union's, or at least the euro area's fiscal capacity, back on the agenda.

Since the mid-1990s, the constraints set by the fiscal framework of EMU and other pressures on national expenditure have made many member states reluctant to accept significant transfers of financial resources to the EU level. Enlargements in 2004 and 2007 have further intensified this trend (see Chapter 19). Although enlargement increased the economic diversity among member states significantly, expansion of the Union-wide redistribution of funds has been strongly opposed by the wealthier member states. In the context of the discussion around a more sustainable EMU, the idea of a euro area budget for stabilization (either within or outside the EU budget) gained some momentum (see Chapter 7). Yet, the fear of permanent transfers led member states to opt for a less ambitious 'instrument for competitiveness and convergence' and to keep the negotiations around it within the context of the new Multiannual Financial Framework. While the Covid-19 pandemic led to an unprecedented fiscal engagement with large-scale borrowing setting a historic precedent, it is not yet clear what will be the lasting impact on the EU as a polity. Three aspects of the political agreement of the European Council in July 2020 are in this respect relevant: first, there is a strong emphasis on the temporary nature of the measures—in line with the legal construction of the package; secondly, almost 90% of the money is paid directly to member states on the basis of national recovery and resilience plans rather than through genuine EU spending programmes (a fact that has been heavily criticized by the EP); and thirdly, almost half of the money takes the form of loans rather than grants.

The major players and hybrid processes

Budgetary policy-making in the Union is a hybrid of different policy modes arising from the diverse purposes of the budget and the treaty provisions and practices that govern macro level negotiations and the annual budgetary cycle. The negotiations that produce the Multiannual Financial Framework (MFF) are an unusual combination of a dominant European Council, a rather powerful Commission because of its agenda-setting role in relation to the overall MFF and the setting of draft MFF regulations, and also a rather powerful EP because of the consent requirement. The dominance of the European Council in MFF negotiations represents intensive transgovernmentalism that occurs whenever the big budgetary packages have to be agreed. The practice of the European Council exemplifies political reality rather than treaty provisions. In fact, the Treaty of Lisbon (Art. 312(2) TFEU) provides for the Council not the European Council, which does not have legislative powers, to adopt the MFF by unanimity after receiving the consent of the EP. The gap between practice and treaty provision underlines the political salience and visibility of the MFF negotiations. The significance of the Commission and the EP in the MFF negotiations is characteristic of the distributional mode of policy, as is the annual budgetary cycle which follows the traditional Community method with a strong role for the Commission in preparing the draft budget, qualified majority in the Budgetary Council, and a significant role for the EP. The day-to-day management of the budget is characterized by a distributional mode that engages many layers of government, from the Commission to central, regional, and local governmental agencies in the member states in a system of multi-level implementation.

The Commission has traditionally been an advocate of a bigger EU budget in order to fund policy integration, but in the 1990s it was forced to pay more attention to managing EU spending. Having repeatedly faced resistance to increasing the budget, the Commission has resorted to options external to the MFF, starting with the European Fund for Strategic Investment (formally established within the European Investment Bank and partly funded by it) and the proposal for a euro area budget (financed potentially by externally assigned revenue) (Becker *et al.* 2017). In addition, the Commission tries to play the role of honest broker in budgetary battles, charged by the member governments with drafting reports on sensitive issues, such as 'own resources' and net flows to the member states. Its role in proposing and implementing the budget has also allowed the Commission to intervene in policy areas that have traditionally been the exclusive domain of the intergovernmental method, such as the establishment of the European Defence Fund within the MFF (Haroche 2019 and see Chapter 17). Similarly, in the context of the Covid-19 pandemic, the Commission skilfully managed to link the discussion on the financing of the recovery with the review of the MFF, thus preventing member states opting for intergovernmental alternatives outside the EU budget framework.

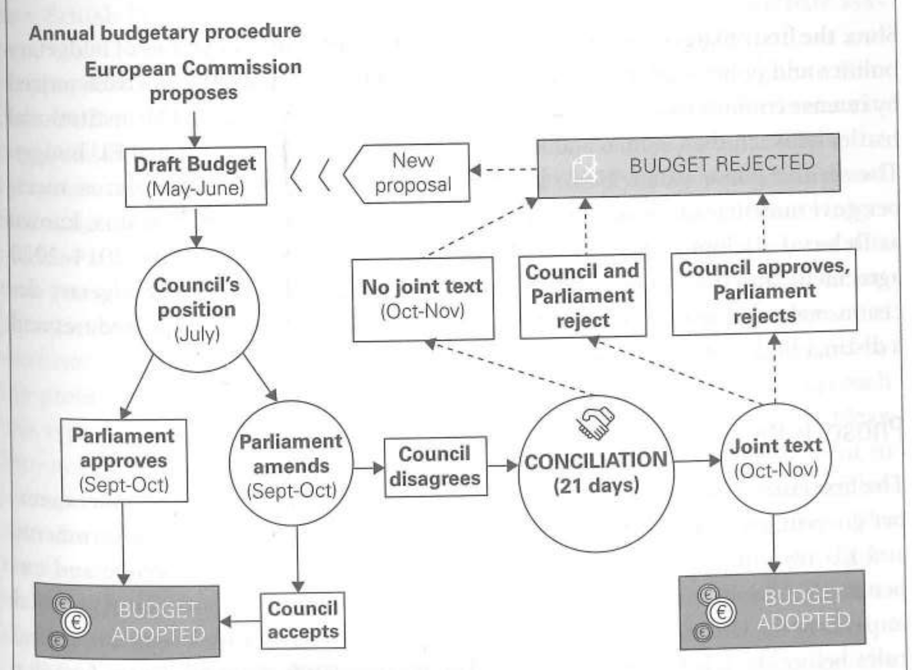
Different configurations of the Council play central roles in budgetary negotiations. The Budget Council, consisting of representatives from finance ministries who approve the annual budget, has well-established operating procedures and decision-making rules. The General Affairs Council (GAC), the Economic and Financial Affairs Council (Ecofin), and the Agriculture and Fisheries Council (AGRIFISH) each play a key role in negotiating the big budgetary deals. However, the European Council, where heads of state or government broker the final stages of the 'history-making' bargains, still provides the most important forum for striking the big budgetary deals. Unlike the annual budget procedure, where the Council de-

frame for EU budgetary politics for a seven-year period—thus limiting the degree of flexibility—but also the scope for potential conflict in the decision-making process for the annual budgets.

Since it was granted budgetary powers in 1975, the EP has regarded EU finances as one of its key channels of influence vis-à-vis the Council. The EP has tried to influence what happens at both the big bargains and the annual fine-tuning. In the annual cycle of determining detailed appropriations, the EP frequently intervenes to alter the sums assigned to specific programmes and projects. The ToL incorporated significant changes to the treaty provisions on budgetary decision-making. Yet, the main elements of the 'new' budgetary procedure reflected the existing inter-institutional agreement (Bauer *et al.* 2018). While Lisbon thus largely constitutionalized the existing modus operandi (see Figure 9.2), the treaty changes had over time noticeable effects, in particular on the influence of the EP in spending decisions which have arguably decreased (Becker *et al.* 2017; Benedetto 2013; Høyland and Crombez 2015).

Under the ToL, both arms of the budgetary authority have equal decision-making power over all components of the EU budget, including CAP spending, in the annual budget procedure. Similar to the co-decision procedure in legislative politics, a Conciliation Committee features as the key forum for brokering deals between the EP and the Council before their respective final readings. These seemingly innovative features were much in line with the informal arrangements that were in place prior

FIGURE 9.2 The budgetary cycle, rules, and practice according to the Treaty of Lisbon



Source: European Commission 2018

to the ToL. Given that negotiations at the conciliation meeting cover all areas of the budget, the distinction between compulsory and non-compulsory expenditure had become less relevant over time. Under the ToL, the Council may prevent an agreement in the Conciliation Committee and thus trigger a new budget proposal by the Commission.

With regard to the financial perspective, the ToL institutionalized the procedures for the multiannual budget plan (as laid down in the inter-institutional agreement) requiring a unanimous decision in the Council and the consent of the EP. If no agreement is reached, the ceilings of the previous multiannual budget plan remain in place. There is thus a strong lock-in effect in the rules because any significant change would require the agreement of all member states and the EP.

The shift from soft law (inter-institutional agreements) to the hard law of the treaty also raises the stakes for the EP in the negotiations of the financial perspective. Since the EP can no longer renounce the financial perspective once it has agreed to it, there is an incentive for it to bargain hard on the terms of the seven-year budgetary deal, as it did following the February 2013 European Council (see later in the chapter).

The EP's role in the supervision of financial management has also been pronounced. In March 1999, the EP's criticism of the Commission's financial management provoked the unprecedented resignation of the whole college of commissioners.

Budgetary politics over time

Since the first enlargement in 1973, there have been two distinct phases of budgetary politics and policy-making in the EU. The first phase (1973–88) was characterized by intense conflict about the size and distribution of EU monies, and by institutional battles between the Council and the EP over the adoption of the annual EU budget. The second phase (since 1988) has been one of relative budgetary calm as member governments succeeded in negotiating the five big budgetary bargains, known as Delors-1, Delors-2, Agenda 2000, the 2007–13 framework, and the 2014–2020 agreement, and the Council and the EP cooperated closely in annual budgetary decision-making. Each phase corresponds to a specific set of rules and procedures and a distinct budgetary paradigm.

Phase 1: the dominance of budgetary battles

The first enlargement disturbed the budgetary bargain established by founder member governments. In particular, between 1979 and 1984, the member governments and EU institutions were locked into a protracted dispute about revenue and expenditure, which contributed in no small way to a wider malaise and lack of political impetus in the Union during the early 1980s. The 1970 treaty was designed to fix the rules before the UK became a member. The revenue sources suited the six founder countries, and the main spending would flow 'automatically' to support the CAP

for starting accession negotiations with the UK and the other applicants. The rules of the budgetary game were fixed to the advantage of the incumbents, above all France, making confrontation with the UK more or less inevitable (see H. Wallace 1983).

Moreover, with the 1970 budgetary treaty, member states half-heartedly delegated budgetary powers to the EP, introducing a complex annual procedure with a number of ill-specified rules. The mismatch between the limited desire of member states to involve the EP and the high expectations of members of the EP (MEPs) due to their newly acquired political powers soon became apparent. The considerable scope for interpretation left open by the vaguely defined treaty provisions intensified this tension. In short, both the UK and the EP entered a budgetary stage that was characterized by a 'de Gaulle budget', a budget that was formed by French preferences with an almost exclusive focus on agricultural spending.

After accession, successive British governments struggled to get the budget issue on to the agenda and slowly managed to alter the terms of the debate to ensure that distributional issues were taken seriously. Despite being one of the 'less prosperous' member states, the UK was set to become the second largest contributor after Germany. In trying to address the problem, a key concern of British governments was the dominance of CAP expenditure (constituting 70% of the budget), from which the UK, with its small 'agricultural sector', benefited very little. The European Regional Development Fund, which was set up in 1975 to stimulate economic development in the least prosperous regions (see Chapter 10), brought only little relief.

Against this background, it became clear to the British government that the UK problem was structural rather than the result of chance. Hence in 1979, the new British Prime Minister, Margaret Thatcher, began to demand a rebate system, which would guarantee the UK a better balance between contributions and receipts. The Commission and the other member governments were loath to concede the British case at the outset. The Commission had always been reluctant to engage in discussion of the net financial flows to the individual member states, lest this encourage too narrow a calculation of the benefits of Union membership, and lead states to seek *juste retour*, in other words to extract from the Union budget more or less what they put in.[3] The key 'orthodoxy' regarding the budget at this time was that receipts flowed from EU policies and were thus automatic. The implication of this approach was that the consequences for individual member states were not regarded as an issue to be addressed. This orthodoxy was challenged by the problem of UK contributions. Although Thatcher's confrontational approach was regarded as non-*communautaire*, she finally succeeded. At the Fontainebleau European Council in June 1984, the British government traded its agreement to increase the VAT ceiling from 1 to 1.4% for the establishment of a 'rebate' mechanism for dealing with excessive British contributions on a longer-term basis. The mechanism was designed to deal with the British problem and could not be generalized to other member states, even though other states subsequently became significant net contributors.

While the member governments were engaged in restructuring the budget, the EP and the Council were involved in a continuing struggle over their respective interests (i.e. essentially raising its role in decision-making and expanding the budget). The EP rejected the 1980 and 1985 draft budgets, and the annual budgetary cycle was characterized by persistent struggle between the two institutions, the 'twin arms' of the budgetary authority. The EP actively exploited the broad scope for interpretation that the ill-specified treaty provisions offered. By contrast, the Council sought to limit the level of power-sharing with the EP as far as it legally could. In 1982 (case withdrawn), and again in 1986 (Case 34/86), the Council brought an action in the Court of Justice of the European Union (CJEU) to annul the budget signed by the President of the Parliament as it disagreed with the EP's interpretation of the treaty provisions on the classification of expenditure (compulsory versus non-compulsory). Repeated attempts to solve the disputes over the interpretation of the treaty provisions through joint declarations and agreements failed.

Phase 2: ordered budgetary decision-making

The year 1988 marked a turning point. After the accessions of Greece, Portugal, and Spain and the adoption of the Single European Act (SEA) (see Chapter 5), it became clear that the intense annual budgetary battles with long negotiations into the night, pressing uncertainty on whether the financial year could start with an adopted budget, and the constant shortage of revenue could not continue. Following a proposal by the President of the Commission, Jacques Delors, the EU embarked on a far-reaching political and institutional reform in the budgetary field.

On the institutional side, it introduced the multiannual financial perspective, which balanced revenue and expenditure and constrained the ballooning CAP by dividing the budget into different headings and setting annual ceilings for spending categories across a five-to-seven-year period. Although established by member states in the European Council, the financial perspective acquired its binding nature from the inter-institutional agreement between the Council, the EP, and the Commission. The EP accepted the constraint on annual budgetary decision-making, because the new financial perspective guaranteed a significant increase in resources and established regional spending as the second-largest part of the budget, both long-standing EP priorities.

Overall, the 1988 reform changed the rules of the game by supplanting the budget treaty with a set of superior soft-law arrangements among the budgetary actors. Annual decision-making lost its place in the inter-institutional spotlight and became the domain of budgetary experts, who cooperated closely and developed a routine of adopting annual budgets on time and without major tensions. Moreover, the 1988 reform transformed the CAP-centred 'de Gaulle budget' into the 'Delors budget' that, due to its strong regional policy dimension (see Chapter 10), was more redistributive and less CAP-oriented.

In subsequent renewals of the financial perspective and inter-institutional agreement, the main institutional and distributive structure established in 1988 persisted. The requirement for unanimity did not change. The Delors-1 package and subsequent budgetary deals required the agreement of all member states. The national veto made it very difficult to challenge entrenched budgetary gains, such as the British budgetary rebate or the French demands on agriculture

The introduction of the multiannual framework did not mean that conflict and disputes disappeared. However, tensions among member states or between the EP and the Council were kept at a manageable level during the annual procedures and channelled towards the renegotiation points of the large budget packages every five to seven years. At these renegotiation points, all players were assured that the unanimity requirement would allow them to block a package that would run contrary to their fundamental interests. This had not been the case in pre-1988 times: key players, such as the UK government, had to fight long and hard until their distributive concerns were addressed, and frequently recurring budgetary disputes prevented the orderly adoption of annual budgets.

Delors-1

The budgetary agreement reached in February 1988 was a classic EU package deal (see Table 9.1). The fact that, for the first time, all the different elements of the budget were addressed in one reform was instrumental to the agreement. Moreover, the link to the ambitious single market programme and related institutional reforms (in the form of the SEA) motivated the German Chancellor, Helmut Kohl, in particular, to secure an agreement, even though it meant a significant increase in Germany's net contributions to the budget. For the poorer member states, such as Greece, Spain, and Portugal, that did not benefit so much from CAP expenditure, a significant strengthening of cohesion spending was a prerequisite for agreeing to an internal-market project that would pose more challenges to their economies than to those of wealthier member states (see Chapter 10).

Delors-2

The pattern established by Delors-1 was replicated in the negotiations on Delors-2. The political link between the SEA and Delors-1 was followed by a similar link between the Treaty on European Union (TEU) and the Delors-2 package. Again, poorer member states established the link between an increase in cohesion spending (i.e. the creation of a new cohesion fund) and further economic integration (i.e. the introduction of EMU).

The debate on Delors-2 was as tortuous and controversial as that on Delors-1. The member governments grappled with their desire to reach agreement, on the one hand, and with their determination that the terms of the agreement be as favourable as possible to their own viewpoint, on the other. At the 1992 Edinburgh European Council, an agreement was reached (see Table 9.1).

Agenda 2000

In the mid-1990s, the balance of forces in the Union on budgetary matters began to change radically. The sizeable expansion of the budget led to the emergence of a 'net contributors' club, a group of member governments concerned about the level of their financial commitments to the EU budget. At the Copenhagen European Council in 1993, the member governments had accepted the principle of an eastward enlargement of the Union. The accession of so many comparatively poor states would

TABLE 9.1 The main elements of the financial perspectives between 1988 and 2013

	Delors-1	Delors-2	Agenda 2000	FP 2007–13	MFF 2014–2020
Revenue ceiling	Rise to 1.2% of GNP by 1992 and an extension of the system of 'own resources' to include a new fourth resource based on the relative wealth of the member states as measured by GNP	Unchanged for 1993 and 1994, but rise to 1.27% of GNP by 1999	Unchanged at 1.27% of GNP	Unchanged at 1.24% of GNI (which is a recalculation of the 1.27% of GDP) with average actual spending level of 1.05%	Slight decrease to 1.23% of GNI. High Level Group of Own Resources established to support potential reform
UK rebate and other correction mechanisms	Continuation of the complex Fontainebleau rebate system	UK rebate maintained; slight adjustments for other net contributors	UK rebate maintained; slight adjustments for other net contributors	UK rebate maintained; slight adjustments for other net contributors	UK rebate maintained; slight adjustments for other net contributors
CAP	Limiting the growth of agricultural expenditure at not more than 74% of GNP	Implementation of 1992 CAP reform (no significant change)	Only limited changes in the size and policy structure of the CAP	Implementation of 2003 CAP reform (no significant change in level of expenditure)	Limited reduction in CAP spending
Cohesion expenditure	A doubling of the financial resources available to the less prosperous regions of the Community	Significant increase in the flows to the poorer parts of the Community	Flows to cohesion countries were marginally reduced, leaving some scope for flows to the new member states after eastern enlargement	A shift of regional expenditure from old cohesion countries to recently acceded countries	Limited reduction in cohesion spending

Against these developments, it is surprising that the institutional setting and the distributive character of the budget proved so robust. The status quo was by-and-large confirmed, but, in contrast to the significant increases recorded in 1988 and 1992, the Union's budgetary resources were consolidated, with no major increase in the size of the EU budget. The new member states were still not at the table and thus had little impact on the negotiations (see Table 9.1).

The Financial Perspective for 2007–13

The negotiations of the 2007–13 financial perspective took place against the background of three developments. First, at the Lisbon European Council in 2000, the EU set itself the strategic goal of becoming 'the most competitive economy in the world' by the end of the decade. Heads of state or government committed to take measures that would increase the competitiveness of their economies and raise investments in research and technology. The Lisbon goal was taken up by a report of an independent group of high-level experts headed by the Belgian economist, André Sapir (Sapir *et al.* 2004). The report strongly criticized the dominance of the CAP spending and suggested refocusing the budget on European public goods, most importantly research and technology. Although fiercely criticized by some in the Commission, the report clearly established a link between the Lisbon goal and the EU budget. Secondly, most member states, in particular the large euro area members, Germany and France, were experiencing low growth rates and strong pressures on their national budgets. Their failure, in three subsequent years (2002–04), to meet the terms of the Stability and Growth Pact (SGP), which commit members of the euro area to compliance with the Maastricht criteria (see Chapter 7), further limited their willingness to accept increases in the EU budget. Thirdly, for the first time, the ten new member states sat at the negotiation table with high expectations of budgetary transfers and a full veto right.

The negotiations for the financial perspective began in early 2004 with a proposal by the Commission. Romano Prodi, then President of the Commission, emphasized the need to give the EU the resources to match its political priorities. The Commission sought to transform the redistributive 'Delors budget' into a more distributive 'Lisbon budget' that would strengthen expenditure for public goods and reduce the emphasis on redistributing resources to poorer regions/member states or to farmers. For the first time since the inception of the financial perspective in 1988, the Commission envisaged an overhaul of the expenditure headings so as to reflect the new policies and priorities of the enlarged EU.

Finding an agreement was again not easy. Essentially, three key cleavages dominated the debate. First, net contributors were unwilling to accept an increase in the spending level, while governments from beneficiary member states, such as Spain and Portugal, stressed the continued importance of pursuing the objective of 'economic and social cohesion' (see Chapter 10). Secondly, among the beneficiaries of regional expenditure, 'old' beneficiaries wanted to prevent an abrupt ending of transfers and demanded compensation, while the new member states feared that these compensation payments would be financed by cuts in transfers to them. Thirdly, replacement by a generalized mechanism, which was naturally favoured by all the other net contributors.

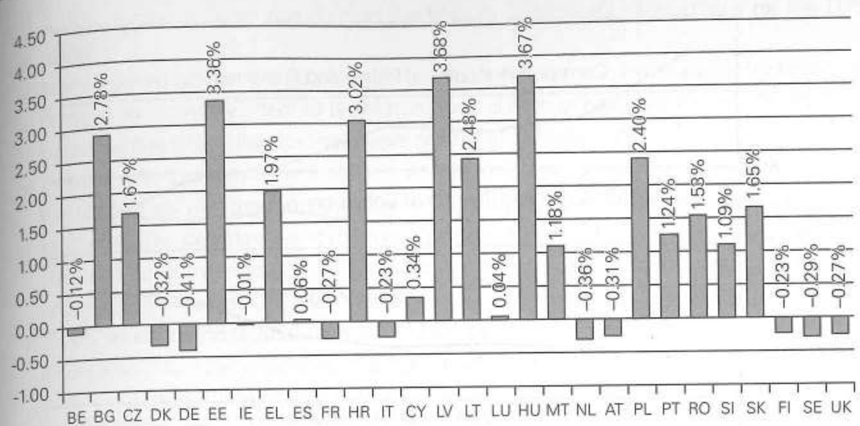
Significantly, the Commission's ambition to strengthen expenditure for public goods found very few active supporters, except the EP. There was little space left for new spending programmes in fields such as innovation and technology, given that agricultural expenditure was excluded from the negotiations (under a Franco-German agreement concluded in 2002) and that regional expenditure was dominated by strong vested interests in the new and old member states. An agreement was finally reached in late 2005 which broadly retained the status quo (see Table 9.1). However, the 2007–2013 MFF negotiations marked the beginning of a gradual evolution of the budget from a negotiation tool aimed at compensating member states for their political compromises to a policy instrument aimed at solving EU-wide problems (Kölling 2019).

Multiannual Financial Framework 2014–2020

The negotiations on the 2014–2020 financial perspective took place against the backdrop of the continuing euro area crisis, the emergence of deep economic divergence within the euro area, and growing differentiation within the EU arising from the challenge of developing the institutions and policy toolkit for managing a single currency (see Chapter 7). The Commission presented its first set of proposals for the future finances of the Union entitled 'A Budget for Europe 2020' in June 2011 (Commission 2011). The emphasis in the proposals was on the value-added of spending at the EU level with a focus on an innovative budget designed to address pan-European challenges, particularly growth and employment (Molino and Zuleeg 2011). The Commission sought a commitments budget of €1,025 billion (1.05% GNI) and a payments budget of €972 billion (1.01% GNI) over seven years. The proposals looked for increases in spending on competitiveness, infrastructure, citizenship and security, and 'global Europe'. The proposals were designed to shift EU spending from agriculture and cohesion to other policy areas in ways that would test the status quo bias of budgetary politics in the Union. The negotiations took place in multiple fora, including unsuccessfully at the November 2012 European Council. The member states finally reached agreement at the European Council in February 2013, but a tense and difficult period of negotiations with the EP followed. Herman Van Rompuy, in his role as European Council President, was the major institutional player during the end-game of the negotiations, working closely with the Commission to mould an agreement.

The member states were divided into three main groupings. The net contributors (see Figure 9.3), consisting of Austria, Finland, Denmark, Germany, the Netherlands, and the UK, sought to limit their contributions favouring a *status-quo* or even a *status-quo-less* outcome. The second group was composed of the newer member states from central and eastern Europe led by the Polish Prime Minister, Donald Tusk. The new member states were primarily interested in the two traditional expenditure policies: agriculture and cohesion. The third group—consisting of France, Greece Italy, Portugal, and Spain—was committed to a larger budget than was acceptable to the net contributors, which would support economic growth in addition to maintaining agricultural and cohesion spending. These states wanted a

FIGURE 9.3 Budgetary balances by member state, 2019



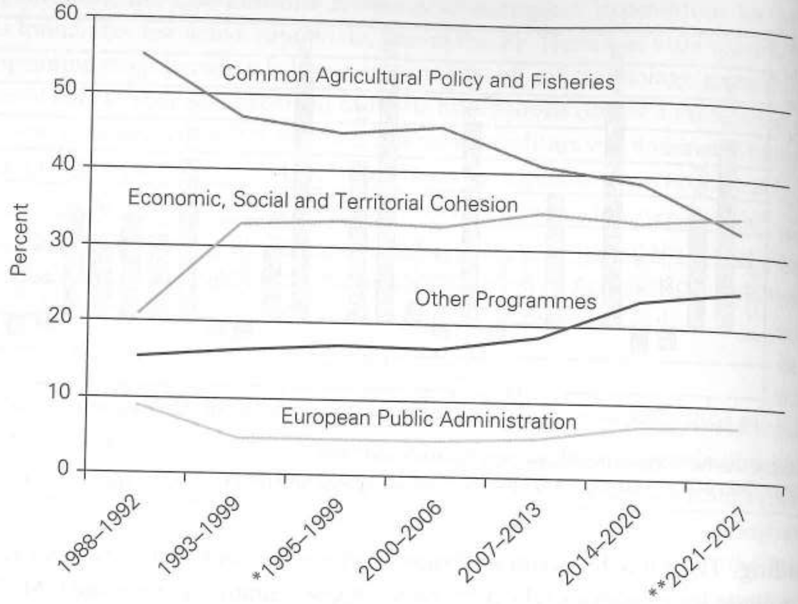
Source: Author elaboration based on Commission 2019 (http://ec.europa.eu/budget/graphs/revenue_expediture.html)

spending. The French President, François Hollande, was torn between promoting policies for growth and the deep-seated French commitment to the CAP. Other countries, such as Belgium and Ireland, did not fall decisively into any one of these camps, but sought to get a deal they could live with by focusing on particular issues.

The EP was also able to assert itself in the negotiations gaining both concessions from an institutional perspective and highlighting its concern about the social dimension of the European project ahead of the forthcoming 2014 EP election. Despite the protracted negotiations, MEPs approved the MFF (2014–2020) and an accompanying interinstitutional agreement in November 2013 (see Figure 9.4 for evolution of main policy areas).

Notwithstanding the high politics of budgetary negotiations and the powerful forces that oppose a larger financial capacity for the Union, there have been important developments in EU finances as the member states have developed further policy instruments to support the single currency. The June 2012 Van Rompuy report and its subsequent follow-up reports in October and December 2012 on creating a Genuine Economic and Monetary Union, as well as the Juncker report three years later, made reference to a number of policy instruments with budgetary implications (Van Rompuy 2012; Juncker 2015; and see Chapter 7). Among the most salient were the creation of a single resolution mechanism as part of a banking union that would be supported by backstop, a reference to financial support for euro area member states that enter a contractual arrangement on structural reform, and reference to the possibility of creating a 'limited fiscal capacity' in the euro area to deal with economic shocks (Van Rompuy 2012). This was further reinforced by the ambitious policy agenda that French President Emmanuel Macron brought forward in 2017 (Macron 2017). It had the creation of a discretionary euro area budget as one of its central proposals, but also sought to advance discussion on

FIGURE 9.4 The evolution of main policy areas in the EU budget



*Adjusted for 1995 enlargement
**Author calculations based on European Council Conclusions in July 2020

Source: European Commission 2018 (https://ec.europa.eu/commission/sites/beta-political/files/euco-budget-booklet-june2018_en.pdf)

Protracted negotiations at the level of finance ministers and heads of state or government finally yielded (rather limited) progress in December 2018. An agreement was found to create a fiscal backstop for the single resolution fund in the form of a credit line at the European Stability Mechanism (ESM) and the euro summit committed to establishing a 'budgetary instrument for convergence and competitiveness' in the context of the MFF for euro area member states. While in 2019 the Eurogroup further implemented this political agreement, it was put on hold (for the ESM-related elements) and overtaken by developments around the Covid-19 pandemic and the sizeable recovery package whose main part, the Recovery and Resilience Facility, borrows features from the euro area budget instrument but has an EU-wide coverage.

Multiannual Financial Framework 2021–2027

In spring 2018, the Commission presented its proposals for the future finances of the Union entitled *A Modern Budget for a Union that Protects, Empowers, and Defends* (Commission 2018*d*). Reacting also to the effect that Brexit would have on the EU finances (see Box 9.2), the Commission proposed a long-term budget of €1.135 billion in commitments, equal to 1.11% of post-Brexit EU GNI. These figures represented an increase in absolute terms from the previous MFF, but a decrease as a share of EU GNI. Total allocations were, in any case, below 1.3% of EU27 GNI, the level

BOX 9.2 Brexit's implications for the EU budget

The UK's departure from the EU had political and financial implications for the EU's budget.

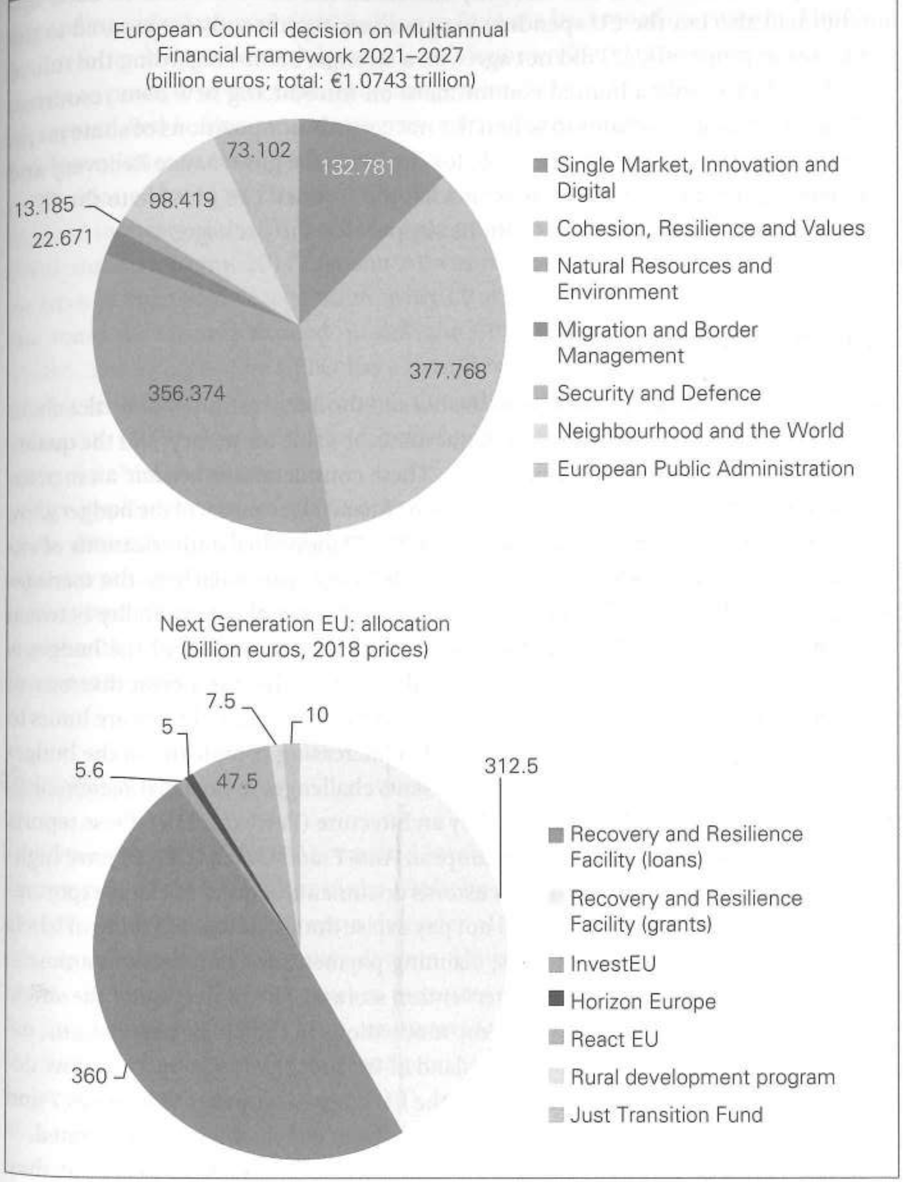
- **Brexit-related gap in the EU budget:** as the UK has been a net contributor to the EU budget, the primary effect of Brexit has been a hole of between €10 and €12 billion annually (i.e. €75 billion for the whole period of the new MFF).
- **Divorce bill:** the withdrawal agreement aligned the UK's de facto participation in the EU budget with the length of the MFF, ending in 2020. The total divorce bill, which also includes payment of outstanding commitments and the financing of some liabilities as at the end of 2020, amounts on a net basis to an estimated amount of around £33 billion or €43 billion (House of Commons Library 2020).
- **EU-UK relations post-2020:** should the UK opt for (and be granted) participation in certain Union programmes, the rules laid down in the MFF for the participation of third countries would apply. These rules distinguish between (1) EEA countries, acceding countries, candidate countries, and potential candidates; (2) countries covered by the European Neighbourhood Policy; and (3) other third countries. For this last group, they foresee an agreement that would lay down the conditions applicable to the participation of the third country concerned in any programme; and the agreement 'should ensure a fair balance as regards the contribution and benefits of the third country participating in the Union programmes, not confer any decision-making power on these programmes and contain rules for protecting the Union's financial interests'.
- **Offsetting contributions from EU27 member states:** in its MFF Proposal, the Commission had stressed that '[in light of Brexit,] maintaining a level of support that matches our ambitions across policy areas will require additional contributions from all member states in a fair and balanced way'. Options to offset the Brexit-related budget hole included increasing national contributions, cutting spending, or creating new revenue sources (see also Schratzenstaller 2019).
- **Budget negotiations:** Brexit changed the political equilibria in budget negotiations. The UK had been a historical supporter of a small budget and of the system of rebates. In the negotiations for the new MFF, this role was taken over by the so-called 'frugal' member states, that is, the Netherlands, Austria, Sweden, and Denmark. At the same time, the absence of the UK at the negotiating table may well have facilitated opting, in the context of the Covid-19 pandemic, for a large-scale fiscal response through the EU budget and based on debt issuance.
- **Flexibility instrument to cope with consequences of Brexit:** the European Council in July 2020 reached an agreement on the introduction of a Brexit Adjustment Reserve of €5 billion which—outside the ceilings of the new MFF—is aimed at countering unforeseen and adverse consequences in member states and sectors that are worst affected.

In line with the previous MFF proposal, the proposed 2021–2027 MFF included significant re-prioritizations in favour of pan-European challenges that had gained more importance, particularly migration, defence, and innovation. Such terms respectively, as well as to an internal re-focusing of cohesion spending. In her 'Agenda for Europe', newly elected Commission President Ursula von der Leyen expressed her intention to steer the budget towards new priorities, including climate change, border management, external action, youth mobility, and the rule of law—coming into line with the proposal from the previous Commission (Von der Leyen 2019*b*). The MFF negotiations following the 2018 Commission proposal to early 2020 followed the pattern of previous budgetary negotiations, underlined by the failure of the new European Council President, Charles Michel, to secure the agreement of the member states at a special EU budget summit in February 2020. The failed summit was overtaken by the arrival of Covid-19 in Europe, which transformed the context and substance of the MFF negotiations.

While at first the measures taken in reaction to the Covid-19 pandemic were adopted at the national level, the EU budget dimension quickly gained pace as the pandemic spread. Consensus grew on the need for a concerted European response both for the more short-term fiscal measures and for the financing of the recovery. The Commission—after smaller sums had already been activated within the existing budget—presented a proposal for a €100 billion loan-based scheme for member states, called SURE, to support unemployment-related costs. The scheme would be financed by issuing debt backed by national guarantees. After intense debates among member states, this proposal was adopted in June 2020, together with two other instruments: a Pan-European Guarantee Fund from the European Investment Bank, which also used national guarantees to mobilize up to €200 billion; and a Pandemic Crisis Support for health-related costs of up to €240 billion, based on the Enhanced Conditions Credit Line for euro area member states under the European Stability Mechanism. In parallel, discussion started on the financing of the recovery, with strong calls from the hardest hit member states for sizeable financial resources, in view of the limited fiscal space that many of them had for increasing their national debt levels and fears of widening divergences within the Union. The European Council in April asked the Commission to prepare a proposal in the context of the EU budget, together with a new proposal for the Multiannual Financial Framework (2021–2027). In addition to the size of such European support, two key aspects dominated the debate on which the Commission had to take a stance, namely whether the Union should issue debt on a large scale, and whether such issuance should finance only loans, only grants, or both loans and grants. In mid-May, France and Germany intervened forcefully, with a call for the creation of a €500 billion recovery fund, and positioned themselves in favour of the issuance of grants.

In mid-May 2020, the Commission presented its proposals for a revamped MFF package and a recovery instrument. The Commission package consisted of two elements: the MFF 2021–2027 amounting to €1.1 trillion over seven years (taking the state of negotiations in February 2020 as the basis) and the *Next Generation EU* instrument of €750 billion entirely funded by borrowing from the capital markets (European Commission 2020*a* and *b*). The key elements of the *Next Generation EU* proposals were: a Recovery and Resilience Facility of €560 billion to be disbursed as both grants and loans, a further €55 billion for cohesion policy, and a Just Transition

FIGURE 9.5 The new MFF 2021–2027 (agreement by the European Council in July 2020)



In July 2020, in a four-day mammoth meeting of the European Council, a political agreement was reached (see Figure 9.5). In particular, the strong resistance of the group of member states called the 'frugals', namely the Netherlands, Austria, Sweden, and Denmark (with support from Finland) over the share of loans negotiations. With reference to its veto right on the adoption of the new MFF, the EP reacted to the agreement negatively and criticized, in particular, the fact that the European Council (1) had not only increased the share of loans to €360 billion but had also cut the EU spending programmes significantly (compared to the Commission proposal), (2) did not agree on a stronger stance regarding the rule of law, (3) included only a limited commitment on introducing new own resources, (4) kept the system of rebates to soften the net contributor positions of some member states, and (5) did not foresee a role for the EP in the governance Recovery and Resilience Facility. It remains to be seen what the Council can provide to the EP to address these criticisms and thus gain its support for the package.

Budget management

The struggle for budgetary resources in the EU and the inter-institutional battles about budgetary power initially overshadowed questions of 'value for money' and the quality of the Commission's financial management. These considerations became an increasingly important focus of budgetary politics as the financial resources of the budget grew.

Managing a budget that involves around 400,000 individual authorizations of expenditure and payment each year is a major challenge, particularly as the management of the EU budget is characterized by a fragmentation of responsibility between the Commission and public authorities in the member states: 80% of the budget is managed on behalf of the Union by the member states. There is a great diversity of public management and public finance cultures across Europe, and there are limits to the auditing capacity of a number of states. The increasing complexity in the budget monitoring and control system of the EU presents challenges to financial accountability, and it creates an overall complex policy architecture (Perreau 2019). Press reports and investigations carried out by the European Anti-Fraud Office (OLAF) have highlighted scams involving the forging of customs documents in order to claim export refunds, avoid anti-dumping duties, and not pay excise duties, or the switching of labels on foodstuffs to claim higher refunds, claiming payments for non-existent animals, and putting non-existent food into intervention storage. The protection of the single market has been one of the Union's prime motivations in the Brexit negotiations, especially in relation to the border on the island of Ireland. No one knows with any degree of certainty the level of fraud affecting the EU budget: estimates of between 7 and 10% of the budget are often cited but have never been convincingly demonstrated.

In the 1990s, attempts were made to improve financial management, but they proved insufficient to prevent financial mismanagement becoming an explosive political issue in 1999, when the Santer Commission was forced to resign. The Prodi Commission, which took over in autumn 1999, was given a mandate to reform the Commission services by the European Council. Commission Vice-President Neil Kinnock, who was given responsibility for administrative reform, proposed a White Paper on the Reform Strategy in March 2000 (Commission 2000*a*). Not unexpectedly, reform of financial management and control systems was one of four priorities

Regulation (*Official Journal*, L 248, 16 September 2002) and extensive management changes in the Commission services. The Commission also adopted a stricter approach with the member states, taking the unprecedented step in July 2008 of suspending aid worth over €500 million to Bulgaria because of corruption. The Kinnock reforms have enhanced the regulatory framework and the capacity of EU institutions to practise sound financial management, but the EU budget remains highly fragmented and is dispersed across very many countries and levels of government, which continues to cause problems.

The idea of having a European Public Prosecutor's Office (EPPO) to protect the financial interests of the EU has had a long gestation. The ToL made provision for an EPPO and, in autumn 2017, agreement was reached to proceed with the EPPO on the basis of enhanced co-operation, with 22 member states choosing to participate. The states that have remained outside the EPPO are Denmark, Hungary, Ireland, Poland, and Sweden. The EPPO has a hybrid two-tier structure with a central office at EU level involving the chief prosecutor and delegated prosecutors in the member states. On 14 October 2019, the Council confirmed Laura Codruţa Kövesi as first European chief prosecutor.

The implementation of the temporary Recovery and Resilience Facility will add a new dimension to the management of the EU budget, but also to the European semester process (see Chapter 7). It combines the surveillance of economic policy-making and national plans with the provision of European money and thus goes significantly beyond earlier attempts to combine EU spending programmes with the European semester process.

Conclusion

Budgetary politics in the EU is marked by elements of both continuity and change. The capture of the EU budget in the 1960s by agricultural interests has proved relatively enduring. France, the main defender of the CAP, has been successful in preserving its interests in this policy domain. However, agricultural support has moved decisively since 1992 from market measures to compensation payments, and the funding has started to shift from consumers to taxpayers (see Chapter 8). Cohesion funding assumed a central role in budgetary politics in the late 1980s with the arrival of Spain and Portugal (see Chapter 10). Structural funds remain an entrenched part of the budgetary *acquis*. However, the outcome of the 2014–2020 budgetary negotiations reduced the weight of these big budgetary items for the first time, and the resources devoted to cohesion policy outstripped agriculture, also for the first time. The new MFF for 2021–2027 confirms this trend. At the same time, in the reaction to the Covid-19 pandemic, it is coupled with a significant temporary increase of the EU budget in the form of financial support for member states based on national recovery and resilience plans.

Agreement in 1988 to the Delors-1 financial perspective represented a step change in how EU budgets were drawn up. Since 1988, multiannual bargains have negotiations have marked all six budgetary bargains outlined in this chapter, the political process, characterized by a set of integrated Commission proposals, intensive negotiations across a range of Councils, and high-level bargaining in the European Council, demonstrated a capacity to frame an outcome that would enjoy broad consensus. The new recovery fund does not fundamentally challenge this conflict-reducing patter of big bargains as it is temporary in nature as a crisis response and fully linked to the new MFF. At the same time, it has the potential to put EU budgetary politics onto a new distributive and institutional path. For the first time, the Union has recourse (temporarily) to large-scale debt issuance and thus becomes the largest supranational issuer. Secondly, the financial support to member states through the Recovery and Resilience Facility follows a different budgetary procedure and introduces a new form of financial support linked to the European semester. Thirdly, the envisaged introduction of new own resources might provide some structural shifts on the revenue side away from the dominant focus on GNI contributions. Thus, it will be interesting to see whether, at the end of the four years when most of the payments of the recovery fund will have been made, a discussion on revamping the existing MFF will take place.

While there will then be the strong status-quo bias—in terms of both institutional structures and the preferences of the major actors—that has long prevented significant changes in the distributive order of the Union, the creation of the recovery fund shows that also in a future crisis the Union is again likely to react together forcefully. It also creates a new distributive and institutional reality that, depending of the economic developments in member states, is likely to induce heightened expectations and interdependencies. It may also provide for another opening in EU budget terms for the discussions on increasingly salient issues, such as climate change, the digital transformation, and other developments on the global stage, and could possibly alter the so far more muted dynamics around the need for a central fiscal capacity for stabilization purposes in the currency union.

NOTES

1 This chapter draws on the EU budget chapter by Brigid Laffan and Michael Shackleton in the fourth edition. Michael Shackleton's consent is gratefully acknowledged. Valuable research assistance was received from Valentina Caracci. The views expressed in the chapter do not necessarily reflect those of the European Central Bank.

2 On the redistributive and stabilization capacity of the EU budget, see in particular Fuente and Doménech (2001), Asdrubali and Kim (2008), and Citi (2017). The latest analysis by Pasimeni and Riso (2018) finds that the redistribution and stabilization achieved by the EU budget in terms of equalization and smoothing of income per capita are low.

3 The impact of these corrective measures is, however, not clear-cut. Citi (2017) shows that rebates have had little, if any, effect on member states' net fiscal position vis-à-vis the rest of the EU, and in some cases, they have produced a result

FURTHER READING

A comprehensive volume on the EU budget is Laffan (1997). Lindner (2006) presents a thorough institutionalist analysis of EU budgetary decision-making over three decades. For an analysis of the revenue side, see Begg (2005) and De Feo and Laffan (2016). For recent analyses on developments in EU Finances and decision-making, see Becker, Bauer, and De Feo (2017) and Benedetto and Milio (2012). For a recent multidisciplinary collection of studies on the features and challenges of the EU budget, see Zamparini and Villani-Lubelli (2019).

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CHAPTER 10

Cohesion Policy

Doing More with Less

John Bachtler and Carlos Mendez

Summary

EU cohesion policy aims to reduce economic, social, and territorial disparities through investment programmes and projects aligned with EU strategic objectives and implemented under a unique model of multi-level governance. It accounts for a major share of the EU budget. This chapter reviews the evolution of cohesion policy over successive reform phases, how the policy is implemented, and the evidence for its effectiveness. It also discusses the different policy modes encompassed in the policy, and it reviews recent political developments relating to politicization, Brexit, the sectoralization of EU spending, and the implications of the Covid-19 pandemic. The chapter concludes that the resourcing, priorities, and governance of cohesion policy for 2021-2027 represent a new turning point in the prospects for the policy, following the strategic turns of 2006 and 2013. Despite growing political concern about inequality in the EU (reinforced by the Covid-19 pandemic), the policy's importance is diminishing as a result of budgetary pressures, greater centralization of political decision-making within the Commission, a fragmentation of the political constituencies for cohesion policy, and the dominance of rival EU policy priorities with more centralized delivery mechanisms.

Introduction

EU cohesion policy aims to strengthen economic, social, and territorial cohesion by reducing territorial inequality and promoting 'harmonious development' at different spatial scales across countries and regions. The policy accounts for the second largest share of the EU budget (some €350 billion in 2014–2020). While it represents less than 0.4% of EU GDP, the policy provides significant funding for public investment in economic development—equivalent to 8.5% of government capital investment in the EU over the 2015–17 period, increasing to 41% for the less-developed EU13 countries.

Implementation is undertaken through 'shared management' between the Commission, member states, and sub-national authorities, involving thousands of implementing bodies and beneficiary organizations. Interventions are supported through a mix of funds to serve multiple EU objectives, and they cover many areas of EU and domestic policy—infrastructure investment, business development, research and innovation, human resources, environmental sustainability, and poverty alleviation.

The significance of cohesion policy for students of policy-making in the EU is threefold. First, it is the most redistributive EU policy area of the EU budget; a core attribute of redistributive policies is the generation of conflictual politics over the size and allocation of funding. Secondly, it is the paradigm case of EU multi-level governance. The policy's partnership principle requires vertical and horizontal interactions between governmental and non-governmental actors at EU, national, and regional levels in the design and implementation of programmes and measures with wider consequences for territorial relations. Thirdly, the performance and effectiveness of the policy in contributing to its objectives of growth, convergence, and regional development, as well as wider EU added value, are heavily contested.

The evolution of cohesion policy has witnessed a number of 'turning points' (Manzella and Mendez 2009). The landmark 1988 reform introduced the core governing principles of concentration, programming, partnership, and additionality supported by a substantial budget. The next major turning point was the 2006 reform, which introduced a more strategic and performance-oriented governing framework that was strengthened under the 2013 reform. For the 2021–2027 period, we argue that the reforms represent another major turning point, reducing the policy's importance and cohesion rationale through a diminished budget and redistributive focus, greater funding conditionality, and a stronger role for the European Council through EU budget negotiations and the European semester.

This chapter explores the evolution of cohesion policy and contemporary developments for the future. The first section focuses on the phases of reform over the 45-year history of the policy. A second section discusses the evolving modes of policy-making encompassed by the policy. The major recent political developments influencing the policy—politicization, sectoralization, and Brexit—are reviewed in the third section. The chapter concludes with reflections on the policy's future,

From minor fund to major instrument of policy and governance

Origins and the landmark reform

The European Regional Development Fund (ERDF) was established in March 1975. While the 1957 Treaty of Rome acknowledged regional disparities and a vague aspiration to reduce them, it did not provide for the establishment of regional policy instruments. There had been calls for the creation of a regional policy by the Commission and some member states throughout the 1960s. However, the main stimuli were twofold: early moves towards economic and monetary union (EMU), which was expected to increase regional disparities; and the first enlargement to include Ireland and the UK, given that both countries were committed to the creation of a Community regional policy to address their development challenges and because of the UK government's aim to improve its budgetary balance with the Community (Flockton 1970; Wallace 1977).

The ERDF was initially a small fund and controlled mainly by member states in accordance with their own regional policy approaches, with limited Community added value. The budget of the Fund was 1.3 billion European Units of Account[1] over a three-year trial period (1975–78), representing around 5% of the Community budget (Talbot 1977). Reforms in 1979 and 1984 and the creation of a new regional policy instrument, the Integrated Mediterranean Programmes (IMP), gradually increased the Fund's budget to some 3 billion European Currency Units (almost 9% of the Community budget), enhanced its Community orientation by granting the Commission more control, and provided a blueprint for the governance of the funds under a major reform in 1988 (Mawson *et al.* 1985).

In the context of major treaty reform, enlargement, and the adoption of the single market programme, the 1988 reform marked the arrival of cohesion policy as a core common policy in its own right underpinned by a treaty commitment to cohesion, a substantial budget, and a common governance framework for all three Structural Funds: the European Regional Development Fund (ERDF), the European Social Fund (ESF), and the Guidance Section of the European Agricultural Guidance and Guarantee Fund (EAGGF) (Marks 1992). Building on the experience of the ERDF and IMPs, at the core of this governance framework were the principles of:

- *concentration* on less developed regions;
- *programming* through multiannual strategies for the 1989–93 period in line with the multiannual EU budget;
- *partnership* to involve sub-national governments and economic and social stakeholders; and
- *additionality* to ensure EU funding did not substitute national funding.

Budgetary consolidation and preparing for enlargement

The timing of subsequent reforms—in 1994 and 1999—was dictated by the EU's Multiannual Financial F

2000–2006 periods respectively (see Chapter 9). The deepening of economic integration had an important bearing on the financial aspects of the reform. The Maastricht Treaty of 1993 provided for the establishment of a single currency by 1999, established economic and social cohesion as a core treaty objective, and created a new Cohesion Fund to support infrastructure development and macroeconomic convergence in the poorest member states. These commitments were reflected in a substantial financial boost to cohesion policy, doubling the 1994–1999 budget relative to 1989–1993. By contrast, for 2000–2006 the cohesion policy budget remained relatively stable, reflecting fiscal consolidation in the run-up to EMU and efforts to contain the anticipated costs of enlargement to Central and Eastern Europe.

The basic regulatory principles of the landmark 1988 reform were retained in the 1994 and 1999 reforms with some changes to respond to EU and national priorities. First, concentration on the poorest EU regions remained a core principle, but additional flexibility was granted to member states in the process of designating assisted areas inside the more developed regions. Secondly, the thematic scope and priorities of intervention were broadened for 1994, while increasing the focus on new EU priorities, for example sustainable development in both the 1994 and 1999 reforms (see Chapter 13) and employment in 1999. Thirdly, the number of Community Initiatives was reduced, responding to criticism from member states about their administrative complexity. Fourthly, programming procedures were streamlined and some management responsibilities were decentralized in response to criticism from member states, particularly under the 1999 reform. Lastly, the importance placed on improving the effectiveness and probity of expenditure increased significantly with strengthened monitoring and evaluation requirements, and the introduction of incentives and sanctions on performance and compliance (Mendez and Bachtler 2011).

The strategic and performance turns

The mid-2000s saw the start of a fundamental change in the positioning of cohesion policy within the EU budgetary and policy frameworks. The 2006 reform, and even more so the reforms for 2014–2020 and 2021–2027, placed increasingly greater emphasis on Structural and Cohesion (Investment) Funds meeting wider EU objectives and required the policy to demonstrate its effectiveness more convincingly (see Table 10.1).

The core strategic change under the 2006 reform of cohesion policy for 2007–2013 was to realign the policy with the EU's Lisbon agenda, which had the stated aim of making the EU 'the most competitive and dynamic knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion' by 2010 (European Council 2000; Mendez 2011). A new strategic planning system was introduced by requiring the design of National Strategic Reference Frameworks (NSRFs) in line with Community Strategic Guidelines (CSGs), links with National Reform Programmes, the earmarking of programme spending to specified expenditure categories, and reporting require-

TABLE 10.1 Evolution of cohesion policy, 1988–2027

Period	EU context	Policy shift	Implementation shifts
1989–1993	Single market programme Enlargement: EU9→EU12	Reform of the Structural Funds—integration into a 'cohesion policy'	Focus on poorest, least developed regions Multiannual programming Strategic orientation of investments Involvement of regional and local partners (partnership principle) EU funding is additional to national expenditure
1994–1999	Preparation for monetary union Enlargement: EU12→EU15	Creation of Cohesion Fund for poorest countries Creation of special objective for sparsely populated regions Doubling of resources	Greater flexibility for spatial coverage Broadening of thematic priorities Decentralization of management responsibilities
2000–2006	Retrenchment in growth of spending Enlargement: EU15→EU25	Agenda 2000—recognition of need to reform Lisbon Strategy—shift of EU priorities to growth, jobs, innovation	Decommitment rule (for faster spending) Stricter monitoring and evaluation rules Emphasis on financial compliance (control and audit)
2007–2013	Adapting to an enlarged EU Enlargement: EU25→EU27/28	Emphasis on policy effectiveness and added value All regions eligible for support	Alignment of cohesion policy objectives with EU goals National strategic documents for cohesion policy spending Ring-fencing of thematic expenditure Strategic reporting Ex-ante financial compliance assessment
2014–2020	Financial and economic crises First reduction in EU budget European semester process	Place-based approach Europe 2020 strategy Focus on policy performance	Performance framework and results orientation Thematic concentration Alignment with EU economic governance Use of conditionalities on spending
2021–2027	White Paper on Future of Europe Brexit Recovery Plan for Europe	Reduction in budget for EU cohesion policy Influence of sectoral EU priorities Links with EU economic governance REACT-EU instrument	Synergies between Funds/policies Further thematic concentration (policy objectives) Mid-term review Simplification of rules Additionality principle discontinued

Changes to the policy architecture included the discontinuation of Community Initiatives, apart from INTERREG (cross-border, transnational, and inter-regional co-operation) which was subsumed within the new Territorial Cooperation Objective. Instruments linked to rural development (the European Agricultural Fund for Rural Development (EAFRD) replaced the European Agricultural Guidance and Guarantee Fund (EAGGF—Guidance Section)) and fisheries (Financial Instrument for Fisheries Guidance—FIFG) were integrated into the CAP (see Chapter 8). There was further decentralization of responsibilities to member states, notably in audit and through needs-based evaluation and a voluntary performance reserve, and wider application of proportionality to selected areas of management. Following the onset of the financial crisis in 2007–08, further regulatory changes in 2009 and 2010 aimed to accelerate spending by improving cash flow and by simplifying some administrative procedures.

The reform of cohesion policy in 2013 for the 2014–2020 period was arguably the biggest reform since 1988, with significant changes to objectives, thematic focus, conditionality, and governance (Mendez 2013). Cohesion policy objectives were aligned more closely with the Lisbon agenda's successor strategy 'Europe 2020' through reinforced strategic programming under a Common Strategic Framework for all shared management Funds (renamed European Structural and Investment Funds—ESIF) and through stricter thematic concentration rules.

More controversially, macroeconomic conditionality was extended from the Cohesion Fund to all Structural Funds empowering the Commission to propose a suspension of funding for breaches in fiscal deficit rules and, for the first time, to request a reprogramming of funding to support the implementation of macroeconomic recommendations (see Chapter 7). This was driven by the Council of the European Union (Council)—particularly Germany, supported by France —and parts of the Commission to promote greater fiscal and budgetary discipline in the aftermath of the euro area crisis, despite opposition from a number of member states, the European Parliament, and the Committee of the Regions.

The performance orientation was enhanced significantly, in line with the proposals of the 'Barca Report', an independent study requested by the Commissioner for DG Regional Policy (DG REGIO), Danuta Hübner, to provide recommendations on the future strategic direction of cohesion policy (Barca 2009). These included a stronger focus on results in the programme strategies; an obligatory performance reserve to reward the achievement of spending targets at the mid-point of the programme cycle; and the introduction of *ex-ante* conditionality requiring institutional, regulatory, and strategic conditions to be met before releasing funds, such as having strategies in place for infrastructure or research and innovation investments. The role of place-based and localized instruments (sustainable urban and community-led local development strategies) and financial instruments (loans, equity etc.) became more important. Lastly, financial management and control were strengthened, along with some simplification.

Throughout the history of cohesion policy reform, the European Commission has been the key architect of reforms to enhance the added value of the policy, often exercising strategic opportunism and policy entrepreneurship (Bachtler *et al.*

Committee of the Regions, which have been strong advocates of a well-resourced cohesion budget, strengthened and extended partnership with sub-national actors in policy implementation, and the promotion of territorial cooperation and localized instruments for community economic development. The European Parliament and the Committee of the Regions have been highly critical of the increasing use of conditionality in cohesion policy as a tool to pursue EU fiscal and budgetary consolidation objectives, but they have been unable to resist reforms in this direction. While supportive of Commission efforts to increase the added value of cohesion policy, the Council has sought increased flexibility in strategic and operational governance requirements in successive reforms to simplify management and reduce administrative burden for beneficiaries of funding. However, such efforts have been offset by the need to respond to new policy objectives and perceived performance deficits as well as demands from the European Court of Auditors and the budget control committee of the European Parliament (EP) to reduce financial compliance weaknesses.

Policy modes: the core distributional mode and emergent modes

Wallace and Reh (Chapter 4) set out a typology of five EU policy modes. In a previous edition, Bache (2015) classified cohesion policy as a 'hybrid' case combining three of the modes of policy-making (Bache 2015): the Community method, the distributional mode, and policy coordination. More recent cohesion policy-making developments are the rise of a new mode of 'intensive transgovernmentalism' linked to wider budgetary decision-making, and an emerging urban agenda under the policy coordination mode.

The *distributional mode* describes an approach to EU policy-making premised on multi-level governance, the empowerment of sub-national actors, redistributive bargaining by member states over the budget, and an increasing legislative role for the EP. The evolving system of multi-level governance at the implementation stage is reviewed in more detail in the next section. Here, we focus on the policy-making stage both in terms of budgetary redistribution and legislative decision-making. Budgetary redistribution is a defining feature of cohesion policy's rationale. It is the only EU budget heading that is allocated largely according to a country's wealth (GDP), so that there is clear redistribution towards poorer member states and regions. All other spending headings, such as the dominant agricultural heading and the growing competitiveness heading, favour wealthier countries.

The politics of redistribution in cohesion policy were evident in the policy's use as a 'side-payment' in budget negotiations throughout the 1980s and 1990s to 'buy' support from poorer member states for further integration (the single market, economic and monetary union, and enlargements) by providing funding transfers to counter competitive disadvantages and adjustment costs that could arise from integration. By contrast, the three reforms in 2006, 2013, and 2020 have seen increased prioritization of non-cohesion headings and instruments under the MFF, putting

downward pressure on cohesion funding and redistribution, and increasing the tensions between net contributors and net recipients (see Table 10.2).

It is notable that the proportion of funding allocated to the less-developed EU regions is now at a historic low (see Table 10.3). In 1989–1993, 73.2% of funding was allocated to so-called 'Objective 1' regions, a figure that fell to 59% in 2007–2013 and most recently 53.5% for 2014–2020. Until the 2000–2006 period, other regions were designated only if they were experiencing problems of industrial restructuring or rural development. From 2007, all regions became eligible for Structural Funds, making funding available to even the most prosperous parts of the EU. This continued into 2014–2020, but combined with a major increase in the proportion of the budget allocated to Transition Regions—including those in Belgium, France, and the United Kingdom which had never previously been designated as less developed. Furthermore, the Commission sought to discontinue the additionality principle in 2021–2027, a core governing principle under the 1988 reform that committed member states to maintain public investments (in less-developed regions only under the 2006 reform) above and beyond cohesion policy funding. Together, these shifts from the mid-2000s onwards indicate that regional disadvantage is playing a diminishing role in the spatial coverage and investment capacity of cohesion policy.

TABLE 10.2 Scale of EU budget and share for cohesion and agricultural policies

Year		Percentage of European Budget[a]		Size of EU Budget[a] as % of GNP or GNI
		Cohesion Policy	Common Agricultural Policy	
Annual budgets	1965	1.4[b]	8.5	0.11
	1975	6.2	70.9	0.53
	1980	11.0	70.9	0.80
	1985	12.8	68.4	0.92
Multiannual Financial Frameworks	1988–1992	22.4	56.2	1.20
	1993–1999	34.1	46.9	1.25
	2000–2006	34.7	44.3	1.09
	2007–2013	35.7	42.3	1.12
	2014–2020	33.9	38.9	1.00

Source: European Commission (2000*b*) The Community Budget: Facts in Figures, 2000; European Commission (2007*c*) EU Budget 2006—Financial Report; European Commission (2014*b*) EU Public Finance, Fifth Edition

Notes: (a) Outturn in payments for annual budgets 1965–1985, appropriations for commitments for multiannual Financial Perspectives from 1988 onwards. GNP from 1988. (b) The 1965 budget corresponds to the ESF created in 1962. The 1975 and subsequent budgets include the newly created ERDF as well as the other Structural Funds (ESF and EAGGF guidance section).

TABLE 10.3 Distribution of funding between categories of region, 1989–2020 (%)

	1989-93	1994-99	2000-04	2004-06	2007-13	2014-20
Less Developed Regions (LDR)	73.2	61.6	63.6	63.2	59.0	53.5
Transition Regions	0.0	0.2	2.6	2.0	7.5	10.8
More Developed Regions	23.6	27.4	24.3	19.1	12.9	16.5
Cohesion Fund (CF)	3.1	10.8	9.4	15.7	20.7	19.2
LDR and CF	76.4	72.4	73.1	78.9	79.7	72.8
Total	100	100	100	100	100	100
EU	EU12	EU15	EU25	EU25	EU27	EU28

Source: European Commission (2014) *Investment for Jobs and Growth*, Sixth report on economic, social & territorial cohesion

A second trend is the increased recourse to budgetary conditionality by making cohesion policy payments to member states conditional on compliance with wider EU fiscal and economic governance rules (Coman 2018; Bachtler and Mendez 2020). Efforts to extend conditionality to the acceptance of migration quotas during the migration crisis and compliance with the rule of law in 2021–2027 have been politically contentious and divisive (Box 10.1).

The rise of conditionality in cohesion policy since the crisis has exposed new elements of '*intensive transgovernmentalism*' (Chapter 4), given the more active involvement of the European Council supported by the Council with a more limited role for the Commission and the EP (Bachtler and Mendez 2020). In the 2013 reform, this was reflected in the stronger role of the European Council in shaping the cohesion policy regulatory framework by issuing conclusions on the MFF that impinged directly on the competence of the co-legislators (Council and Parliament) over the substance of the cohesion policy regulatory package. This related mainly to the provisions on macroeconomic conditionality, eligibility, the links with the Connecting Europe Facility, the performance reserve, and co-financing rates. The EP has been critical of the increased activism of the European Council in setting the parameters of budgetary and regulatory decisions relating to cohesion policy as part of MFF negotiations, which it argues has impinged on the EP's co-legislative competences (Bachtler and Mendez 2016; see also Chapter 8 for similar trends in the common agricultural policy).

The *Community method* is also a key mode of cohesion policy-making. The European Commission's power of initiative grants it sole responsibility for drafting

BOX 10.1 Rule of law conditionality

Conditionality linked to the rule of law is a controversial proposal that has received considerable media attention in the context of debates about a weakening of democratic institutions in Poland and Hungary. In 2018, the Commission tabled a formal proposal on 'the protection of the Union's budget in case of generalized deficiencies as regards the rule of law in the Member States' (COM(2018) 383), applicable to various EU instruments under both centralized and shared management. In the case of shared management funds, a range of financial sanctions are proposed where there is a risk of a generalized deficiency in the rule of law in a member state:

- a suspension of the approval of one or more programmes or an amendment thereof;
- a suspension of commitments;
- a reduction of commitments, including through financial corrections or transfers to other spending programmes;
- a reduction of pre-financing;
- an interruption of payment deadlines;
- a suspension of payments.

The sanctions would be applied where the deficiency risks affecting EU financial management and interests such as:

- public procurement or grant procedures;
- the proper functioning of investigation and public prosecution services in relation to the prosecution of fraud, corruption, or other breaches of EU budget law;
- the effective judicial review by independent courts of actions or omissions; the prevention and sanctioning of fraud, corruption, or other breaches of EU law relating to the implementation of the EU budget; and the imposition of effective and dissuasive penalties on recipients by national courts or by administrative authorities;
- the recovery of funds unduly paid; and
- effective and timely cooperation with the EU fraud and prosecution offices.

The Commission would propose such measures to the Council, which would make a decision based on a reversed qualified majority vote, and the measures would be lifted once the deficiency was remedied or ceased to exist.

to determine reform principles and content. The Commission begins the process by setting out proposals for reform as part of the negotiations on the EU budget for the period ahead, covering all EU budgetary headings, of which cohesion policy is one; and legislative proposals for the implementation of cohesion policy instruments, in the form of draft regulations. Once the Commission has published its proposals, the negotiation and adoption of the budget and regulations are the responsibility of the Council and the EP. Since the 2009 Lisbon Treaty, the EP has had full co-decision powers over all the cohesion policy regulations, providing it with greater scope to shape legislative outcomes, although it remains the junior partner over financial

The *policy coordination mode* is a less documented but increasingly salient mode in two main areas of cohesion policy. The first is coordination of member states' own economic policies with cohesion policy. While such coordination was always an EU treaty commitment, formal mechanisms for coordination were introduced only through the EU's Lisbon agenda, its successor Europe 2020 strategy, and the overarching EU economic and fiscal policy coordination cycle (the European semester), which issues Country-Specific Recommendations (CSRs) (see Chapter 7).

European Union cohesion policy has been increasingly integrated into these policy coordination mechanisms through requirements to address relevant CSRs in cohesion policy programming and implementation, and to earmark funding to EU priority themes. For the first time, the 2019 European semester country reports included a section dedicated to cohesion policy, providing Commission views on priority investment areas and conditions for effective implementation of 2021–2027 cohesion policy in each member state. This realignment arguably weakens the emphasis on cohesion in terms of reducing regional disparities, given the lack of a spatial focus to EU economic and fiscal policies and their centralized mode of operation (Begg *et al.* 2013; Mendez 2013).

The second main area of policy coordination is urban and spatial planning, which operates outside of the Community method in an intergovernmental setting (Faludi 2004). The increasing importance of an EU Territorial Agenda addressing urban and spatial policies in a coordinated and multi-level manner has received impetus with the addition of a territorial dimension to EU cohesion objectives under the Lisbon Treaty. The renaming of DG REGIO as the 'Directorate-General for Regional *and Urban* Policy' (emphasis added) in 2012 is also indicative of this shift. Yet, the EU has no formal competence in the field of urban development or spatial planning. Resembling the open method of coordination in other policy domains lacking EU competence, intergovernmental dialogue and peer review are the main coordination mechanisms involving periodic informal meetings of ministers for urban and spatial policies with technical support provided by various working groups and networks. The Territorial Agenda 2020 approved under the Hungarian EU Presidency in 2011, and its 'renewal' under the Austrian, Romanian, Finnish, and German EU Presidencies in 2018–20, have set out policy frameworks for territorial cohesion, but implementation is dependent on (uneven and inconsistent) member-state commitment and action. In the urban context, a key milestone was the 2016 Pact of Amsterdam establishing the Urban Agenda for the EU, which set out a series of actions delivered through thematic partnerships. However, a coherent EU urban policy remains absent, owing to the lack of a firm EU legal framework and the fragmented urban institutional and policy landscape across EU member states (Atkinson and Zimmermann 2016).

The distributional mode as a shifting system of multi-level governance

Cohesion policy is one of the main EU policy areas implemented through 'shared management', along with the common agricultural policy (see Chapter 8) and the

policy, the allocations to member states, and the eligible areas are proposed by the Commission and decided by the European Council, subject to the consent of the European Parliament as part of the negotiations on the MFF (see Chapter 9). The regulatory framework is again proposed by the Commission and co-legislated by the Council and Parliament. Implementation of cohesion policy is the responsibility of member states through a mix of national and regional multiannual funding programmes, with the Commission ensuring compliance through a mix of conditionalities and sanctions.

The balance of decision-making power between the Commission and member states, and between national and sub-national actors within member states, has been extensively studied over the 30-year life of cohesion policy (Bachtler *et al.* 2013). At the policy design stage, the development of policy proposals by the Commission shifted over a period of time from a closed and relatively secretive process within the main Directorates-General for Regional and Urban Policy (DG REGIO) and Employment and Social Affairs (DG EMPL) to a more open process where DG REGIO 'conscripted' member-state officials through various fora such as 'high-level groups' to debate and test policy proposals. Within the Commission, DG REGIO was often highly influential as an 'early mover' of policy ideas and concepts (notably for the 2006 and 2013 reforms) which subsequently shaped—to a significant degree—the content of the budgetary and policy proposals in the MFF. The reverse was true in the development of proposals for the 2021–2027 reform (Commission 2018*c*), which was conducted centrally by a small group within the Juncker Commission, with a much more restricted role for DG REGIO and less accessibility for member-state officials.

Both during the process of policy development, and more so during the negotiation phase, the main cleavage among member states has historically been between so-called 'net contributors' (those paying more into the EU budget than they get back in receipts) and the 'net recipients'. The composition of the two groups has shifted over time in the MFF. Among the net contributors, the UK was traditionally the most 'hard-line' in pushing for a lower EU budget and less spending on cohesion policy during the 2000s. The UK was supported most prominently by the Netherlands and Sweden, and less publicly by Austria and Denmark (Bachtler *et al.* 2013); following Brexit, these four countries—dubbed the 'frugal four'—became more outspoken in making the case for budgetary restraint. Among the net recipients, the southern EU member states, notably Spain and Italy, tended to be most active in promoting more spending up to 2005, a role also taken on by Poland thereafter. Alliances among member states have tended not to be durable, with each country eventually seeking the best deal for itself in the final stages of the negotiations (Allen 2010). The exception has been the group of central and eastern European countries that joined in 2004 and 2007.

With respect to the implementation of cohesion policy, academic interest was driven by the landmark reform of the Structural Funds in 1988 and the perceived reshaping of territorial governance with a greater role for the Commission and sub-national actors. Marks (1993: 392) identified the Structural Funds as 'the centralized functions of the state up to the supranational level and some down to the local/regional level' representing a challenge to the centralized approach to decision-making within some member states and state-centric accounts of EU decision-making.

The challenge for research is that the relationship between the Commission and member states is constantly evolving, with a regulatory framework that is adapted in each funding period in the light of implementation experience and external pressures (from the Council, Parliament, or European Court of Auditors). Further, the regulations invariably leave scope for interpretation, with member states frequently requesting advice from the Commission. This in turn leads to guidance from the Commission, which national and regional authorities feel obliged to follow (i.e. a form of soft law).

Under the early regulatory frameworks for 1989–1993 and 1994–1999, member states had considerable leeway to determine how, when, and where the funding was allocated. The Commission was mainly entrusted with ensuring that member-state programmes had a justified development strategy, a financial plan, and mechanisms for ensuring funding was spent on eligible expenditure. The subsequent regulations for 2000–2006, 2007–2013, and 2014–2020 progressively gave the Commission more control over different aspects of implementation, as it sought to enhance its strategic role in shaping implementation outcomes and to counter criticism about weak policy performance and value for money, especially by net contributor countries (Mendez and Bachtler 2011; Bachtler and Ferry 2013; Bachtler and Mendez 2020).

In the 1999 regulations, the European Commission sought to accelerate the pace of spending with the introduction of the decommitment rule, requiring that funding committed to projects was paid out within two to three years or else would be lost to the programme. A series of new regulations from 2003 onwards tightened control of financial management and audit to prevent the high level of compliance mistakes ('irregularities') found in audits of cohesion policy expenditure by the European Court of Auditors. In 2006, the first EU requirements were introduced to 'earmark' a minimum percentage of funding to specific thematic priorities reflecting overall EU objectives. A step further was taken in the 2013 regulations which set out a list of 11 thematic objectives on which funding had to be concentrated, subsequently repackaged into five policy objectives for 2021–2027 (see Table 10.4). Lastly, the 2013 regulatory framework incorporated a wide-ranging set of obligations relating to programme performance—the need to justify spending according to an 'intervention logic', the application of performance targets, and the specification of policy and institutional pre-conditions that needed to be in place (*ex-ante* conditionalities) before programmes were approved by the Commission.

Research during the 1990s sometimes sought to assess changes in regulatory frameworks in terms of Commission versus member-state gains or losses of influence. For example, the 1994–1999 regulations were presented as a 'renationalization' of the policy in some cases (Hooghe and Keating 1994). In fact, it was truer to say that the locus of Commission influence shifted over time, moving from decisions on *financial inputs* in the 1990s to *implementation* during the 2000s to *outcomes* in the

TABLE 10.4 Cohesion policy objectives

2014–2020 Thematic objectives	2021–2027 Policy objectives
1. strengthening research, technological development, and innovation	1. a smarter Europe by promoting innovative and smart economic transformation
2. enhancing access to, and use and quality of, ICT	2. a greener, low-carbon Europe by promoting clean and fair energy transition, green and blue investment, the circular economy, climate adaptation, and risk prevention and management
3. enhancing the competitiveness of SMEs, of the agricultural sector (for the EAFRD) and of the fishery and aquaculture sector (for the EMFF)	3. a more connected Europe by enhancing mobility and regional ICT connectivity
4. supporting the shift towards a low-carbon economy in all sectors	4. a more social Europe implementing the European Pillar of Social Rights
5. promoting climate change adaptation and risk prevention and management	5. a Europe closer to citizens by fostering the sustainable and integrated development of urban, rural, and coastal areas and local initiatives
6. preserving and protecting the environment and promoting resource efficiency	
7. promoting sustainable transport and removing bottlenecks in key network infrastructures	
8. promoting sustainable and quality employment and supporting labour mobility	
9. promoting social inclusion, combating poverty and any discrimination	
10. investing in education, training, and vocational training for skills and lifelong learning	
11. enhancing institutional capacity of public authorities and stakeholders and efficient public administration	

Source: https://ec.europa.eu/regional_policy/en/

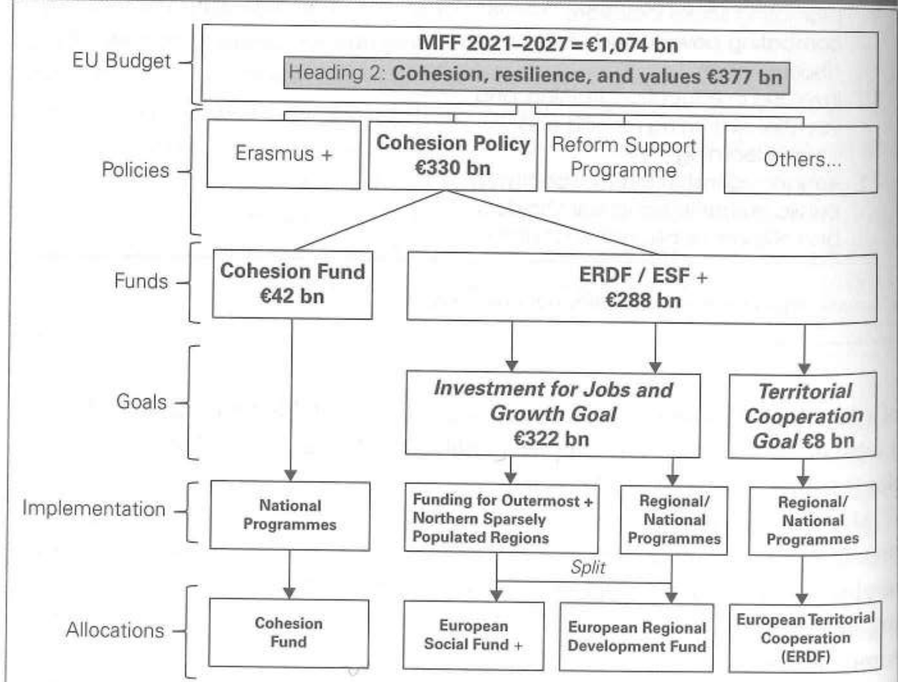
of a 'layering' of regulatory requirements, as shown in Table 10.1, that have built up a substantial administrative compliance obligation for national and regional authorities (Mendez and Bachtler 2011; 2017).

Member-state resistance to the scale and scope of regulations has led to growing pressure on the Commission for the 'simplification' of rules, pleas for 'differentiated implementation' (meaning fewer regulatory *obligations*) from member states receiving smaller amounts of funding, and threats (that have so far not materialized) from some member states to withdraw from the policy due to 'high administrative cost' (see Chapter 8 for similar trends in the common agricultural policy). The establishment of a High-Level Group on Simplification in 2015–17 was a high-profile effort by the Commission to respond to these concerns and rationalize the regulatory re-

The 'programming principle' requires member-state authorities at the start of each funding period (currently with a duration of seven years) to draw up multiannual programmes setting out their strategic objectives and priorities for the use of funding—in areas such as business development, infrastructure, research and innovation, human resources, and environment. They also specify the management systems for allocating the funding to 'beneficiaries' and the financial control systems for ensuring the correct use of expenditure. Following adoption by the Commission, the 'managing authorities' designated by member states to implement the programmes then allocate funding to eligible projects up to the end of the funding period, with a further two to three years thereafter for expenditure to be paid out. The structure of budget headings in the MFF (proposed for the 2021–2027 period) and its allocation to funds and subsequent programmes are shown in Figure 10.1.

Under the so-called 'partnership principle', the cohesion policy regulations require that national and regional development programmes are designed and implemented through a collaborative process involving authorities at regional and local level, economic and social partners, and organizations from civil society to ensure that interventions are adapted to regional and local needs. The range of partner types to be involved has expanded over time in EU regulations, and the reform in 2013 introduced a code of conduct to encourage more active participation of stakeholders.

FIGURE 10.1 The financial allocation process for cohesion policy



Source: Authors' elaboration adapted from ECA (2019: 12)

Reference: ECA (2019) Allocation of Cohesion policy funding to Member States for 2021–2027. Rapid case review, March 2019, European Court of Auditors (www.eca.europa.eu/lists/ecadocuments/rcr_cohesion/rcr_cohesion_en.pdf)

Although partnership applies to all stages of the programme implementation process, the most important element is arguably the participation of regional and local authorities (and non-governmental actors) in so-called 'monitoring committees' which member states are required to put in place to ensure that cohesion policy funding is correctly implemented. The practice varies significantly across (and within) member states, determined mainly by national institutional structures and traditions (Bache 2015).

In the early years of the policy, the regulatory provisions made for involvement of regional and local authorities were seen as a radical step. Leonardi and Nanetti (1990) argued that the increased role for regions meant that they were 'no longer excluded from direct participation in the process of European integration'. However, participation does not necessarily translate into influence. Some have argued that central governments remained the dominant actor with a 'gatekeeping' role between EU pressures and domestic policy and institutional change (Anderson 1990; Pollack 1995; Allen 2005; Bache 1998, 1999). It was recognized early on that there were significant variations in sub-national involvement in cohesion policy across countries—and across different stages of the programming cycle—reflecting the influence of national systems of territorial relations (Hooghe 1996; Marks 1996). Regions that were already strong domestically, as in federal Belgium and Germany, were more able to take advantage of new structural-fund opportunities. Research on the Europeanization of territorial governance in Central and Eastern Europe in the 2000s found that the impact of the partnership principle on multi-level governance was limited, owing to centralized state traditions and a lack of capacity at sub-national level (reviewed in Bache 2015; see also Bachtler and McMaster 2006; Bachtler *et al.* 2014; Dabrowski 2014).

National government ministries of finance, economy, or regional development, or designated development agencies, are responsible for managing or coordinating implementation in most countries. In some centralized countries (as in Greece and Portugal), national management is organized through regional offices of the state. Only in Belgium, France, Germany, Italy, the Netherlands, Poland, and (pre-Brexit) the UK is there significant devolution of management to regional self-governments (or city authorities in a few cases, such as Prague and Rotterdam). Elsewhere, regional authorities are involved as 'intermediate bodies' with delegated authority for functions such as project generation and selection, as in Finland and Romania, or wider programming responsibilities (Spain).

These implementation arrangements are not static. For example, Poland progressed from having a series of 'thematic' programmes and a single 'integrated regional programme' in 2004–06, to having decentralized programmes run by regional offices of the state (*voivods*) in 2007–2013, to devolved programmes managed by regional self-governments in 2014–2020. France has also progressively transferred the management of cohesion policy from prefectures to regional councils. The Czech Republic regionalized cohesion policy management for 2007–2013 but then recentralized it for 2014–2020. A process of centralization and rationalization of cohesion policy administration over time is also evident in Denmark, Finland, and Sweden, as

Controversies and challenges

The performance and effectiveness of cohesion policy have been a subject of controversy throughout the policy's history, partly due to the methodological difficulties in establishing the contribution of the policy to growth and convergence across the EU. This has increased the pressure on the Commission to improve the evidence base for its assessments and the policy's performance orientation. For the 2021–2027 period, the major political developments influencing the reform of the policy are politicization, sectoralization, and Brexit. These challenges are reviewed in turn.

Policy controversy over effectiveness and added value

The effectiveness of cohesion policy has been fertile ground for research and debate for much of the life of the policy. In terms of the politics of cohesion policy, the focus on effectiveness is attributable to three factors (Bachtler *et al.* 2013). First, the significant increases in the EU budget agreed in 1988 and 1992, and subsequent smaller increases in 1999 and 2005, raised the net budget contributions for richer member states, especially Germany, the Netherlands, the UK, and (from 1995) Austria and Sweden. Secondly, the experience of implementing the Funds in 1989–1993 and 1994–1999, and more so in later periods, was perceived to be increasingly complex and bureaucratic by member states, yet the evidence for policy outcomes was uncertain and contested, with limited monitoring and evaluation data to demonstrate the impact of the Funds. Thirdly, in the course of the 2000s, successive Commission presidents sought to redirect the EU policy focus away from so-called 'old policies' (cohesion policy, CAP) and towards so-called competitiveness policies, such as R&D, initially under the Lisbon Strategy and then its successor, Europe 2020. Given the poor performance of the EU in meeting targets for growth, this argument had considerable resonance across the EU institutions and in some member states and was justified in part by perceived weaknesses in the performance of cohesion policy.

These factors focused policy-makers' attention on the efficiency and effectiveness of cohesion policy, specifically whether economic and social cohesion of the EU had increased, and whether any improvements could be attributed to the Structural and Cohesion Funds. However, for much of the period of the policy—certainly up to the 2000–2006 period—academic research and evaluation of the impact of the Funds faced major methodological challenges, notably the poor availability of regional data on socio-economic indicators and cohesion policy spending, and the difficulty of comparing outcomes with any genuine counterfactual (Polverari and Bachtler *et al.* 2014; Davies 2017). The main macroeconomic models applied to ESIF funding by the Commission—QUEST, HERMIN, and RHOMOLO—tended to find positive effects, especially in the member states where the Funds account for a significant percentage of domestic GDP. Econometric regression analyses—assessing the effect of the Funds on GDP growth or employment—produced much more varied results, some finding effects on convergence but others showing little or no impact, depend-

the leveraging of private sector investment, business development, or net jobs creation also produced differing results. Given the conflicting results, it was difficult to draw definitive conclusions (Ederveen *et al.* 2002; Sapir *et al.* 2003: 78), although much of the research indicated that performance was influenced by the investment mix of Structural Funds programmes and the quality of institutional capacity. The Commission also sought to widen the terms of the debate by referring to the 'added value' of the policy, which encompassed qualitative aspects of the policy's implementation such as the benefits of multiannual planning and partnership, for which there was some evidence of influence on domestic policy thinking and practice (Bachtler *et al.* 2013).

For the 2007–2013 period, a major effort was led by DG REGIO in the Commission to turn around the performance of the policy and the evidence base of the assessments. Substantial investment was made in evaluation, focusing on improving the quality of data collated by member-state authorities, better evaluation methods, and a much wider range of evaluation research. Performance was given a higher profile, with the introduction of a performance framework in the 2013 reforms, and so-called '*ex-ante* conditionalities' required member states to put in place laws, strategies, and institutional arrangements that would improve the policy context and administrative capacity for managing the Funds effectively. In part, this has been successful: much of the more recent research has concluded that the Funds have a positive impact on national and regional economic development (Bachtler *et al.* 2016; Davies 2017).

Changing political context

There are three major political developments in the EU with important consequences for cohesion policy. The first is the rising politicization and indeed contestation of policy-making in the EU. A tendency for policy élites to ignore 'places that don't matter' has contributed to a wave of political populism with strong territorial foundations (Rodríguez-Pose 2018). Accordingly, it is argued that the promotion of better territorial development policies that tap potential and provide opportunities to those people living in 'left behind' places is needed to counter the wave of anti-EU populism (Rodriguez-Pose 2018). However, this has not translated into an EU commitment to strengthen the strategic role and financial capacity of cohesion policy. In fact, the White Paper on the Future of Europe mooted three (out of five) scenarios where cohesion policy would be rationalized (European Commission 2017*f*).

Cohesion policy decision-making has become more politicized in the post-crisis era, and public opinion is playing a more important role in the policy process. While the negotiations of EU cohesion allocations and net budgetary balances are always politicized, the level of political division among member states and across EU institutions surrounding cohesion funding was compounded in the debate on the 2021–2027 EU budget, as attempts were made to link allocations to wider macroeconomic and political (migration and rules of law) goals. Analysis of media stories on cohesion policy over time shows that news coverage of funding conditionality evidence that public opinion is having an impact on decision-making. The Commission's protracted decision to refrain from suspending cohesion funding to Spain and Portugal in 2016 for breaches in fiscal rules under the new macroeconomic conditionality rules was motivated in part by concerns about a negative political backlash in a context of deteriorating trust in the EU.

The second major political development is Brexit, which has serious budgetary implications for the EU27. The loss of a net contributor has involved substantial constraints on the scale of the MFF. Commission advocacy of maintaining spending in 2021–2027 at a similar level to 2014–2020 and phasing out budget rebates implied a sizeable and controversial increase in net payments of other, mainly richer countries. There are also changes in the dynamics of budgetary negotiations as other net contributors (the Netherlands, Sweden, Denmark, Austria), able in the past to let the UK take the lead in calling for budgetary restraint on the size of the MFF and Cohesion budget heading, became more prominent during the MFF negotiations.

Lastly, there is the question over post-Brexit participation of the UK in cohesion policy. Involvement in the Northern Ireland PEACE programme co-funded through cohesion policy under its European Territorial Cooperation strand of funding will continue under the terms of the EU–UK Withdrawal Agreement. However, UK involvement in other EU territorial cooperation programmes, such as INTERREG promoting inter-regional cooperation across European regions, is likely to diminish or cease.

The final major political development is the sectoralization of EU spending. Under the Juncker Commission, administrative reform led to a centralization of political decision-making within the Commission, focused on the Cabinet of the Commission President and Vice-Presidents, which weakened the political profile, influence, and autonomy of cohesion policy. This limited the scope for manoeuvre by the Commissioner for Regional Policy to drive the agenda for cohesion policy reform in 2021–2027, and the policy is increasingly becoming a delivery vehicle for wider EU thematic objectives under the strapline of modernization and the pursuit of synergies across budget headings. In the 2021–2027 MFF, there is a clear shift in priority from shared management to centrally managed policies to provide more scope for Commission influence over spending (Bachtler *et al.* 2019).

These sectoralization and centralization dynamics are also evident in the 2020–23 EU Recovery Plan for Europe agreed in 2020 in response to the Covid-19 pandemic. The proportion of funding explicitly allocated for cohesion purposes under REACT-EU (Recovery Assistance for Cohesion and the Territories of Europe) is sizeable at €47.5 billion but it is a relatively small part of the overall package. It is also notable that the EU decided to provide additional funding to cohesion policy through a time-limited instrument rather than increasing the core cohesion budget. The main priority of the Plan is a Recovery and Resilience Facility (RRF) with a budget of €672.5 billion distributed through loans and grants towards the green and digital agendas. Directly managed by the Commission and with national recovery plans coordinated via the European semester, the RRF has a limited focus on territorial cohesion objec-

Conclusions

This chapter has discussed the evolution of cohesion policy over successive reform phases and explained how the distributional mode is institutionalized and the evidence for its effectiveness. It has also discussed the different policy modes encompassed in the policy and reviewed recent political developments. This final section reflects on the implications for the future role of cohesion policy in EU policy-making.

Taking the long view, it can be argued that the current debate over the resourcing, priorities, and governance of cohesion policy for 2021–2027 represents a new turning point in the prospects for the policy going beyond the strategic and performance turns in 2007–2013 and 2014–2020. In purely budgetary terms, the agreed funding of cohesion policy after 2020—with a projected level of commitments of over €330 billion—would suggest that the policy remains in good health. The MFF recognized that the policy is largely effective in promoting cohesion, and that the less-developed countries and regions have a continued need for the investment supported through the Funds.

There are, however, three factors which indicate a diminution in the importance placed on the policy. First, the recent centralization of political decision-making within the Commission has severely weakened cohesion policy in two ways: by deliberately restricting the room for manoeuvre of the Commissioner for Regional Policy (who was able to initiate and drive reforms undertaken in 2005 and 2013), and by effectively pushing proposals to shift resources from shared management to centrally managed policies. Further, it is remarkable that the increasing profile of inequality in Europe—and its obvious territorial dimension in both political and economic terms—is not reflected in Commission strategic planning. Insofar as the Commission is concerned with cohesion—for example in the White Paper on the Future of Europe (Commission 2017*f*) or the Commission's contribution to the EU's Strategic Agenda 2019–2024 (Commission 2019*b*)—it is with social cohesion not territorial cohesion. The growing importance of the European semester process, and the increasing resources allocated to 'structural reforms' (managed by a new Directorate-General, DG REFORM) are also likely to set parameters on how cohesion policy resources are allocated.

Secondly, there has been a fragmentation of the political constituencies for cohesion policy at EU level and in the member states. Within the Commission, it is notable that the Commissioners and Directorates-General responsible for Employment & Social Affairs and for Agriculture & Rural Development have sought to separate their Funds away from the ERDF, wholly so in the case of the EAFRD (continuing a process already evident in 2013) and partially so in the case of the ESF+. This undermines one of the central pillars of the 1988 reform, which introduced a more coordinated approach to cohesion across all three Funds.

Across the member states, the united approach of the central and eastern European countries to budgetary and regulatory reform under Polish leadership has been and some west European member states. The same is true to a lesser extent in southern Europe: Italy is not the same ally of the Commission and advocate for cohesion policy that it was in 2013.

Moreover, with the loss of UK budget contributions, the net contributors are becoming more assertive about the increased costs of EU spending—especially the Netherlands, Denmark, Austria, and Sweden—exacerbated by continued Commission attempts to phase out national rebates. Pressures on spending under the EU budget in 2021–2027 invariably mean cuts to cohesion policy and the CAP.

Lastly, EU policy priorities are primarily sectoral or non-spatial. Much of the focus at EU level is on completing economic and monetary union and recovery from the Covid-19 pandemic, building new or expanded policies for climate change, technology, defence, immigration, and overseas development. Cohesion policy, along with the CAP, has been repeatedly termed an 'old policy' despite its contribution to key EU objectives relating to regional innovation, connectivity, and the energy transition. The main advantage of cohesion policy is that it has a governance system able to deliver on such EU priorities, but its role has increasingly been prescribed top-down, weakening the ability of countries and (especially) regions to use the Funds for development opportunities and needs that are seen as locally relevant. Perhaps the main challenge, though, comes from the future development of European economic governance for the euro area (see Chapter 7) where some form of territorial compensation mechanism to deal with the effects of asymmetric shocks is likely to be needed. This would pose fundamental questions about the scope and relevance of cohesion policy.

NOTE

1 Former currency unit of the European Communities based on a basket of member-state currencies. Replaced by European Currency Units in 1979 until the creation of the euro in 1999.

FURTHER READING

EU cohesion policy is a constantly evolving policy and is closely intertwined with EU budgetary reform. Bachtler *et al.* (2013) provide a comprehensive analysis of the history and relationship between EU budget and cohesion policy reform, including an in-depth analysis of the negotiation of the 2006 reform. For historical accounts of the implementation of policy principles linked to debates on supranationalism and intergovernmentalism, see Bache (2015) on 'partnership' and 'additionality', and Bachtler and Mendez (2007) on the 'concentration' and 'programming' principles. The classic and foundational study of the partnership principle and the impact on multi-level governance is the edited volume by Hooghe (1996). Further contributions to the multi-level governance debate in Central and Eastern and Southern Europe include Bachtler and McMaster (2008) and Bache and Andreou (2010). The 'Barca Report' (Barca 2009) is a comprehensive study of the place-based rationale

analysis perspectives. A more recent and up-to-date contribution by Mendez *et al.* (2019) analyses the Commission's reform proposals for 2021–27 and the key reform themes on the future agenda.

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