The Commission's propositions for the enlargement negotiations on agriculture, structural funds and the budget: an analysis[*]

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Introduction

In its 2001 Strategy Paper[1], the Commission stated that it might be possible to conclude the accession negotiations with ten candidate countries by the end of 2002. These countries are: Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia. These countries could then become members of the EU by 2004.

For the purpose of monitoring the progress towards membership achieved by every applicant, the Commission has divided the EU's membership conditionality into 30 chapters. At the beginning of 2002, three of the most contentious chapters still have to be addressed : agriculture, structural funds and the budgetary framework. These issues are highly sensitive, as they will determine the cost of enlargement. The closure of these chapters is a precondition for the conclusion of the accession negotiations and the entry of the applicant countries.

In a recently adopted information note[2], the Commission sets out the global approach it intends to propose to the Member States in the future Draft Common Positions. The aim of the present comment is to analyse these propositions. It comprises both a synthesis of the proposed strategy, a critical analysis, and suggestions for change.

1. THE COMMISSION'S PROPOSITIONS

1.1. Agriculture[3]

The Commission's strategy for dealing with the EU's enlargement negotiations on agriculture basically covers three issues: direct payments, rural development and market policy.

1.1.1. Market policy

[*] Updated version of the manuscript of a study published in *Studia Diplomatica*, vol. LIV, Nr 3, 2001, pp. 3-19.
[1] European Commission, Making a success of enlargement. Strategy Paper and Report of the European Commission on the progress towards accession by each of the candidate countries. COM (2001) 700.
[2] European Commission, Communication from the Commission. Information note. Common financial framework 2004-2006 for the accession negotiations. Brussels, 30.1.2002, SEC (2002) 102.
[3] A special issues note is dedicated to this chapter: European Commission, Enlargement and agriculture: Successfully integrating the new member states into the CAP. Issues Paper. Brussels, 30.1.2002, SEC (2002) 95.

For the CAP market policy, the Commission proposes a full application of the acquis for the 10 new Member States immediately upon accession. The candidate countries will also be subject to all the CAP supply management instruments, including production quotas. For their calculation, the Commission proposes to use the most recent historical reference periods for which data are available, i.e. 1995-1999. The Commission believes these statistics are more reliable than those of the pre-transition period. However, those new Member States which opt into the simplified system of direct payments will not be subject to supply control requirements as regards premia ceilings and set-aside. They do remain subject to quota restrictions.

1.1.2. Direct payments

The Commission proposes a gradual introduction of direct payments in the new Member States. It considers that an immediate introduction of full direct payments would freeze the existing structures and thereby hamper the badly needed modernisation of the agricultural sectors in the new Member States. Furthermore, these direct payments are not likely to be employed in productive uses and could create considerable income disparities and social distortions in the new Member States.

Hence, the Commission proposes a transition period of 10 years for the progressive introduction of full direct payments. Direct payments to farmers in the new Member States would start at 25% of the level of support to current members in 2004, and rise to 30% in 2005 and to 35% in 2006. After 2006, direct payments to the farmers in the new member states would be further increased to reach the level of the current Member States in 2013.

However, this could lead to a reduction in agricultural income support in those new Member States, where the national aid granted prior to accession was higher than the direct payments under the phasing-in approach. Therefore, the Commission proposes to grant the new Member States the option of complementing direct aid up to the level applicable prior to accession, provided that the total support does not exceed the level of direct payments in the existing Member States.

The Commission moreover proposes a simplified direct payments system for the first three years, with an optional prolongation of two more years. Under this system, the new Member States will have the option to grant direct payments during a limited period in the form of a de-coupled area payment. An average area payment would be determined for each country on the basis of its national envelope of direct payments and its total utilised agricultural area.

1.1.3. Rural development

In order to foster the necessary restructuring of the new Member States' agricultural sectors, the Commission proposes an enhanced rural development policy that is better adapted to the needs of these countries. The Commission thus proposes a significant increase in financial support for rural development measures. The new

Member States will be able to benefit from a cofinancing rate of 80% instead of 75% for a range of rural development measures.

The Commission also proposes a special measure for semi-subsistence farms in the new Member States. In order to turn them into commercially viable units, a flat rate aid of 750 Euro would be granted to these farms provided that they submit a business plan demonstrating the future economic viability of the enterprise.

1.2. Structural actions

The Commission's proposal regarding the structural actions tries to find a middle ground between on the one hand the big needs of the new Member States in terms of development assistance, and on the other the only limited absorption capacity of these countries. Given these absorption problems, it has been decided in 1999 that the receipts from the structural actions (including the cohesion fund) should be capped at 4% of a recipient country's GDP.

The Commission believes that their absorption capacity could be increased if resources are focused more on cohesion fund expenditure (i.e. expenditure on infrastructure and environment). It therefore proposes envelopes for structural actions based on a share of 33 % for the cohesion fund, compared to 18% for the current cohesion countries. At the same time, the amounts foreseen under the Berlin scenario for structural funds in the first three years of accession (i.e. 2002, 2003, and 2004) and adjusted for 10 new Member States would remain unaffected and thus apply for the first years of accession.

The corresponding aid per capita for structural expenditure in favour of the new Member States would attain 137 euro per capita in 2006, compared to an average of 231 euro per capita for the existing four cohesion countries. These amounts account for 2.5% of total GDP of the new Member States, compared to 1.6% of total GPD of the cohesion countries.

1.3. Budgetary provisions

The agreement reached by the Berlin European Council[4] on the new budgetary framework, as laid down in the Interinstitutional Agreement of 6 May 1999[5], envisaged the entry of six new Member States in 2002 and the corresponding annual amounts. Since enlargement will not take place until 2004 and could include up to ten entrants instead of six, this Berlin scenario has to be adjusted.

In line with the Interinstitutional Agreement, the Commission's proposal remains nevertheless in accordance with the expenditure ceilings agreed in Berlin for each of the years 2004 to 2006. The amounts foreseen for accession in 2002 and 2003 are

[4] Presidency Conclusions Berlin European Council, 25/3/1999, Bulletin EU 3-1999.
[5] OJ C 172, 18/06/1999.

no longer available. They cannot be transferred to later years in view of the annuality of the financial perspective ceilings.

The ceilings of 2004-6 will thus have to accommodate the entry of ten entrants instead of six. As agriculture and structural actions account for 80% of the EU's budget, the necessary adjustments will have to occur in these areas. The Commission believes that its proposals regarding both these issues would allow the financing of an enlargement of up to ten entrants while catering for specific issues.

The budgetary savings in agriculture stem from the adaptation of market-related CAP expenditure to updated forecasts of the agricultural situation. The phasing-in of direct payments limits the budgetary costs of extending them. Under the heading structural actions, money is saved by not taking as a point of departure the amounts foreseen for the years 2004-6, but rather the amounts originally foreseen for the first years of accession of the six entrants. The adjusted amounts are shown in table 1.

Table 1 : Financial Framework for Enlargement 2004 – 2006 (M Euro)

Scenario: Accession of 10 new Member States in 2004	***2004***	***2005***	***2006***
Commitment appropriations			
Agriculture	2048	3596	3933
Structural actions	7067	8150	10350
Internal policies	1176	1096	1071
Administration	503	558	612
Total commitment appropriations	**10794**	**13400**	**15966**
Total commitment appropriations (Berlin 1999 scenario)	*11610*	*14200*	*16780*
Payment appropriations (Enlargement)	**5686**	**10493**	**11840**
Payment appropriations (Berlin 1999 scenario)	*8890*	*11440*	*14220*
PM Budgetary compensations			

These savings would allow the EU not only to respect its budgetary ceilings, but also to cater for some specific issues in the applicant countries. These issues essentially concern: nuclear safety, institution building, and the northern part of Cyprus.

However, the combination of low agricultural and structural transfers during the phasing-in period on the one hand, and a full contribution to the EU's 'own resources' on the other, could seriously threaten the applicants' current net receiver position, to the point of becoming net contributors to the EU for some time after accession.

The Commission acknowledges that this would be highly inequitable given these countries' state of development and the heavy costs of complying with the EU acquis. The Commission therefore proposes to grant them compensatory budgetary payments in the form of lump sums, paid out of the margin under the overall ceiling.[6] Its size would be dependent on the outcome of the accession negotiations.

2. SOME CRITICAL OBSERVATIONS

Comments may be divided into two levels. The first level concerns the different problems covered by the propositions. At that level, the propositions present both positive and negative aspects. The second level concerns the general strategy. From that point of view, the propositions are not satisfactory.

2.1. Agriculture

2.1.1. Direct payments

a) arguments pro and contra

The Berlin framework did not cater for direct payments in favour of the farmers in the new Member States. Several arguments have been forwarded among EU circles not to extend the direct payments to farmers of central and eastern european countries (CEEC):

1) farmers from the accession countries should not receive these 'compensatory' payments as these countries were not EU-members when the price cuts were pursued (their farmers will actually witness price increases for most commodities)[7];
2) these payments would entail huge implementation problems and high administrative costs for the new Member States, which would have to be born by the state budget;
3) these payments will be capitalised in the land prices, the increase of which will benefit (mainly urban) landowners, to the detriment of tenant farmers, and will block the necessary rationalisation of land ownership;[8]
4) these payments affect the choice of agricultural products and will lead to a shift towards highly protected products;
5) the extension of these payment would cause very substantial income disparities between the farmers and the non-farming (rural) population;[9]

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[6] With the accession of Sweden, Finland and Austria in 1995, degressive lump sum payments were granted from 1995 until 1998.

[7] European Commission, Study on alternative strategies for the development of relations in the field of agriculture between the EU and the associated countries with a view to future accession of these countries, (Agricultural Strategy Paper), CSE(95) 607, DGVI and DGI, Brussels.

[8] Buckwell, A., Report of an expert group, Towards a Common Agricultural and Rural Policy for Europe. In: European Economy, Reports and Studies, 1997, no. 5.

6) these payments are bad instruments for fostering restructuring. Direct income payments would consolidate current dualistic structures, without ensuring the investment and restructuring necessary to improve the competitiveness of CEEC agriculture to EU-15 levels.[10]

It should be underlined, however, that most of these arguments (1-4) also apply to current Member States. The first argument is not a satisfactory one, because these payments are now being granted to EU-farmers (new farmers & farmers from Eastern Germany, Austria, Sweden and Finland), who were not farming in the EU at the time of the MacSharry-reform.[11] Administrative implementation costs are large in several current Member States. In the EU-15, direct payments are also capitalised in land values and also determine the product choice. It thus seems that only argument 5 and 6 are valid ones.[12]

Moreover, there are also some arguments in favour of extending direct payments to farmers:

1) not granting them any payments whilst granting payments to EU15-farmers would constitute an infraction of the single market principles as it ignores the question of differential state aids in a common market;[13]
2) related to this, CAP regulations fail to give any legal basis for denying direct payments to some countries and a non-extension may be challenged before court;
3) it would also be highly inequitable as these farmers, who are more in need of support than their western counterparts, would be financing the compensation payments of current EU-15 farmers;
4) direct payments could to some extent provide a substitute for credit market imperfections, as access to credit is problematic in these countries.[14]

In any case, the non-extension of these payments is likely to arouse a strong societal reaction in these countries. In turn, this will have significant political implications. During the accession negotiations, the candidate countries will thus argue forcibly in favour of the extension of direct payments.

b) some positive elements of the Commission's paper

The gradual phasing-in of direct payments avoids the negative implications for the restructuring process and for rural income equality, which an immediate full implementation would entail.

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[9] Pelkmans, J., Gros, D., Nunez-Ferrer, J., Long-run economic aspects of the European Union’s eastern enlargement. Wetenschappelijke Raad voor het Regeringsbeleid, Working Document 109, The Hague, Sept. 2000.
[10] Pouliquen, A., Competitiveness and farm incomes in the CEEC agri-food sectors. Implications before and after accession for EU markets and policies. Published on the Commission’s website, oct. 2001.
[11] Ferrer, J. N., Emerson, M., Good bye agenda 2000 – Hello, agenda 2003. Effects of the Berlin Summit on Own Resources, Expenditures and EU net balances. CEPS, Working Document no. 140.
[12] Swinnen, J., 2001, A Fischler reform of the Common Agricultural Policy, CEPS Working paper 173, 2001, p. 25.
[13] Mayhew, A., Financial and budgetary implications of the accession of Central and Eastern European countries to the European Union. Sussex European Institute, Working Paper no. 33, 2000, p. 12.
[14] Swinnen, J., 2001, op. cit., p. 25.

Moreover, the fact that the Commission grants the new Member States the option to implement decoupled payments is also positive. This will attenuate the administrative implementation problems, as the method allows a simple implementation and control. Its decoupled nature attenuates pressures towards intensification and environmental damages. Furthermore, it facilitates the access of smaller farmers to EU funds and is in that way more equitable than the current system.

Finally, the decoupled nature might also make it possible to place these support measures in the so-called Green Box[15], which would fully exempt them from the reduction commitments regarding domestic support foreseen in the Uruguay Round Agreement of Agriculture (WTO). This is good news, as the Blue Box[16], in which the current EU direct payments are placed, is bound to be challenged during the next trade round and therefore the continued exemption from reduction commitments of this kind of measures is uncertain.

c) some negative elements of the commission's paper

Considering the advantages of a decoupled approach, one wonders why this is only optional and not mandatory. The optional character leaves the door open to the full adoption of direct payments in their current form. The new Member States and agricultural lobbies in these countries will thus lobby hard for this. The Commission's approach has a fundamental flaw : it is bound to add ten new potential adversaries of any fundamental reform of the EU direct payments within the Coucil of agricultural ministers of the enlarged Union.

Instead, the new entrants could be obliged to adopt the decoupled system, with as a quid-pro-quo the promise from the current EU-15 that they would also move in that direction. This would entail that during the upcoming mid-term review the current Member States engage themselve to undertake a phasing-out and decoupling of the current direct payments[17].

Furthermore, this distorsion of competition in the agricultural sector could provoke distorsions in neighbouring sectors, beginning with transformed agricultural products. The basis of the CAP in 1957, meaning the need to have harmonised principles concerning the production of food in the common market, still remains valid.

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[15] Green box measures are deemed to have no or minimal effect on production and trade. They should be provided through a publicly-funded government programme, not involving transfers from consumers, and shall not have the effect of providing price support to producers. The support amount should not be related to the type or the volume of production. In fact, no production shall be required to receive green box support.

[16] Blue box measures are production-linked support measures, related to production-limiting policies. Direct payments under production-limiting programmes are not included in the reduction commitments if they are based on fixed area and yields or made respectively a fixed number of headage, or if they are made on 85% or less of the base level of production.

[17] In that context, a 'full bond system' could be adopted. Swinbank and Tangermann propose to turn the current headage and area payments into decoupled, fully transferable bonds, with 'interest payments' which are possibly degressive over time and modulated. This bond system would give the farmers a guaranteed flow of income. It fosters agricultural restructuring since it removes the incentive for farmers to plant some hectares or keep some animals uneconomically in order to receive payments. It would also remove the burdensome administrative controls. As the bonds would be attached to individuals and not to land/farm, their capitalisation in the land/farm prices would be avoided. In the WTO, it could switch payments from the contentious blue box to the generally accepted green box-measures. Swinbank, A., Tangermann, S., A proposal for the future of direct payments under the CAP. Working Paper 1, prepared under the Commission project Bondscheme, Oct. 2000.

2.1.2. Rural development

The problem with the CAP's rural policy pillar is its biased sectoral approach: it is too much concerned with agriculture sensu stricto, instead of setting up a global approach to rural development. A genuine rural policy involves far more than policies related to land-based activities such as conservation of the environment, landscape and nature. Rather, it should involve employment policies, hard and soft infrastructure, public services etc. This holds especially for the new entrants. In fact, the greatest challenge facing rural regions in Central Europe is to develop healthy economic prospects *outside* the agricultural sector, in industry and services[18]. This priority is not taken enough into consideration by the Commission's propositions.

No clear choice is made in favour of a genuine rural policy. Its focus remains biased towards agricultural processes. This is exemplified by the fact that the increased co-financing rate (80%) applies equally to the so-called 'accompanying measures' as to the 'non-accompanying measures'. The former are rural development measures which are essentially concerned with extensification, production-limiting and the environment, i.e. policies which do not contribute greatly to the development of rural regions in these countries.[19] Non-accompanying measures are policies such as investment in agricultural holdings, training, improvement of processing/marketing, and adaptation and development of rural areas. A differentiated cofinancing rate, favouring the latter, would contribute more to the 'rural revival' of these regions.

Furthermore, the proposed special measure for semi-subsistence farms is unlikely to foster the restructuring of the agricultural sectors of these countries. It will instead hamper the labour outflow from agriculture and the rationalisation of farm structures in the new Member States. In that way, the measure seems hard to reconcile with the Commission's justification for not granting full direct payments, as this would hamper restructuring.

Making these payments conditional on submitting a business plan demonstrating the future economic viability of the enterprise does not alter this evaluation. It is hard to see how (and if) these plans would be used to cater for the restructuring of such farms. In any case, the administrative needs for implementing such a program seem haunting. Again, the optimal solution would have been a full-blood rural regional policy for the new Member States, something for which the structural funds are better equipped.

2.1.3. Market policy

The major negative point here concerns the implementation of production quotas. Given the high administrative costs, it makes little sense to introduce for a short while a complicated policy on the highly fragmented farm structure of the countries of Central and Eastern Europe (CEECs), and then subsequently to abolish it. In any

[18] Wetenschappelijke Raad voor het Regeringsbeleid, Towards a pan-european Union. Reports to the Government No. 59.
[19] Early retirement, support for less-favoured areas, agri-environmental programmes, afforestation.

case, if they are implemented as proposed by the Commission, then it seems that the side of the adversaries of quota-reform within the Council is strengthened. In that way, the Commission's proposal lacks a strategic vision.

Furthermore, if they are implemented and then abolished afterwards, the farmers of the CEECs, which were guaranteed high prices, will face price reductions and will claim with reason compensation payments. The question which emerges here is: at what level will the farmers in these countries be granted these compensation payments and in what way? Will they also start off with the proposed percentages (25%-30%-35%) or will they start at higher levels? In this respect, it should not be forgotten that by then the new member states will also be sitting at the negotiation table.

Moreover, the prices in the CEECs (except for Slovenia) of some commodities covered by CAP are currently lower than EU prices. If these price gaps remain, an issue which remains to be tackled during the accession negotiation concerns the alignment of these prices and the financing of these measures.[20] The Commission's proposal does not address this question.

2.2. Structural actions

The Commission's proposal regarding structural actions seems to be well-balanced. The structural money going to these countries will be limited in the beginning given the phasing-in provisions and the 4%-cap but this can be defended on four grounds.

1) None of the current member states have received transfers above this level from the structural funds.
2) Immediate full access to the funds would lead to macro-economic absorption problems for the accession countries. The cofinancing of structural funds will lead to budgetary problems for the CEECs, which are already facing a tough fiscal climate. If the macro-economic balance is not maintained, the funds might add to inflationary pressures and squeeze out private capital flows, whereas the inflow of funds risks creating 'dutch disease'-problems.[21]
3) The administration of the funds requires well-functioning regional administrative structures, which the new member states do not have for the moment.[22]
4) Structural funds money may (ironically) lead to structural problems: if badly spent, the funds could create a dependency culture, based on rent-seeking behaviour. In this respect, substantial transfers may inhibit indigenous efforts at structural reform.[23]

[20] Pezaros, P., The Agenda 2000 CAP reform agreement in the light of the future EU enlargement. EIPA Working Paper 99/W/02.
[21] Mayhew, A., Recreating Europe, The European Union's policy towards Central and Eastern Europe. Cambridge University Press, 1998.
[22] See: T. Szemlér, Regional development and the EU pre-accession and structural funds. Trends and possible courses of action. Institute for World Economics of the Hungarian Academy of Sciences, Working Paper 110, July 2000. For an overview of the different countries, see: Brusis, M., Central and Eastern Europe on the way into the European Union: Regional policy-making in Bulgaria, the Czech Republic, Estonia, Hungary, Poland and Slovakia. Bertelsmann Foundation & Centre for Applied Policy Research, 1999.
[23] Begg, I., Structural fund reform in the light of enlargement. SEI Working Paper no. 25, 1998, p. 16.

Nevertheless, a rather perverse drawback of the 4% cap is however that among the new Member States the transfers to the better-off would be higher than for the poorer ones.

The proposal to attribute a bigger share to the cohesion fund attenuates the four problems mentioned. In that way, it would have advantages for the new Member States and the old ones. For the *new Member States*, this fund could finance greatly needed infrastructure works and help solve environmental problems. The level of cofinancing for the cohesion fund (85%) would benefit the new Member States, while the project approach and the focus on countries instead of regions would circumvent their administrative problems. For the current *EU-15,* such a fund would allow the current members to be involved in a much deeper way in the use of the structural funds in the new Member States and thus to ensure 'value for money'. The fund could also be used to finance trans-european networks, in which enterprises of the current EU-15 could be involved[24].

However, it can be asked why, given the multiple advantages of the cohesion fund approach, the Commission still bothers to adopt a dual approach of granting aid through both the cohesion fund and the structural funds. This is especially questionable given the small size of most countries involved, which makes a regional approach most of the time irrelevant. Instead, one could opt to only implement a full-blood cohesion fund in these countries until 2006, which in due time could also provide objective 1-support. After 2006, both old and new Member States could then decide on the future outlook of the Union's regional policy.

2.3. Budget

The Commission proposes to implement the contribution rules for the new Member States to the EU budget from the beginning. As the new Member States may legitimately expect not to see their net position deteriorate as a result of enlargement, the Commission proposes to grant them compensatory budgetary payments, paid out of the margin left under the ceilings.

However, no rationale is given why the transition period occurs on the expenditure side. It could be argued that it might be better to grant the new entrants a derogation on the revenue side of the EU budget, i.e. in their contribution to the 'own resources'. For instance, an only gradual transfer of import duties and agricultural levies could be envisaged. To this end, they could be granted a greater share of collection costs, which could enable a learning-by-doing effect. Another option would be a reduction of their payments on the VAT or GDP resource (as was granted to Greece, Spain and Portugal).

Furthermore, this would circumvent a problem related to the implementation of direct payments. Reimbursements from the EU budget for Member States' expenditure on

[24] European Commission, Second Report on economic and social cohesion. Conclusions and recommendations. Adopted by the European Commission on 31 January 2001, p. 13.

direct payments is only made the year after their payment to farmers. There would thus be no reimbursement to the new Member States out of the 2004 budget, while they would be required to fully contribute to this budget and to pay out the direct payments for 2004. They would only be reimbursed from the EU budget in 2005. This is troublesome given the tough fiscal climate some of these countries are already facing, not in the least due to acquis compliance costs as well as restructuring needs. A transition period in their budgetary contributions would ease this problem.

3. THE LACK OF A GLOBAL STRATEGY

The Commission's proposals are largely flawed because they lack a long-term vision for the future. This holds especially for agriculture, but also for some aspects of the structural policies and the budgetary framework. Furthermore, in areas which are in big need of reform (agriculture and the budget), the Commission's proposals do not seem to take into account the impact of the accession of these countries on the decision-making effectiveness in the Council and on the corresponding feasibility of reform. If the possibility of reforming the EU policies before accession is foregone, it will prove even harder (if not impossible) to reform after accession. This holds especially for the CAP, as these countries have big agricultural interests to defend. Obviously, this is linked to the failure to reform the EU's institutional framework at Nice.

3.1. Agriculture

Of course, one should not underestimate the challenge of the present situation. The CAP has been flawed for a long time. With enlargement, the deficiencies of the CAP will be extended eastwards. The EU has now to deal with the fact that it did not reform properly the agricultural policy in 1999, both substantially and financially. The Commission tries to correct some minor deficiencies, but it does not deal with the general problem.

Firstly, it makes a great error by distinguishing the accesion negotiations about agriculture and the internal negotiations on the same topic. This can only engender political problems. Another fundamental weakness of the Commission's proposition is to present agricultural measures for the candidate countries without integrating them in a global perspective about the reform of the CAP. There is no long term vision about direct payments, rural subsidies, and quotas. The project is thus logically and politically difficult to defend. This does not mean that the present Member States would have done better. Nevertheless, it is the Commission's duty to defend the common interest and the long term vision. This has not been done.

The proposition also underlines the unbalanced character of the accesion negotiations concerning the acquisition of land. One knows that the transitory period about this was a burning topic in 2001, among others with Poland. It is highly curious that the EU decided to negotiate this without knowing the form of direct payments in the candidate countries. The value of land is directly dependant on the level of subsidies. Temporary exceptions are thus justified as long as the level of European subsidies is not the same. By ignoring this, the Commission obliged the candidate countries to negotiate from an unequal position.

According to us, the proposition should be more structurally oriented. It can thus be temporarily discriminatory, provided a guarantee of non discriminatory treatment in the future is firmly given to the candidate countries. Nevertheless, a specific conditionality is linked to such strategy. On one side, a similar orientation towards a more structural CAP should be followed in the present Member States. On the other side, strong financial guarantees should be given for the development of rural policy and of alternative employment in the candidate countries. One must not underestimate the fact that the EU is imposing these countries a reform that the Union has never been able to realise with such depth and speed.

3.2. Structural actions

The Commission's proposition is certainly better from the point of view of the structural funds. It increases the role of rural policy (though some modalities may be contested). It opens the possibility to increase the absorption rate. This is nevertheless not a long term perspective, since the financing of the structural funds after 2006 remains uncertain.

The proposition should place, as has already been said, a stronger emphasis on a broad definition of rural development. It could also better take into account the quantum leap in regional diversity that enlargement entails, and the lack of administrative capacity in the accession countries. The absorption of ISPA funds has been illustrative in this regard.

3.3. Budget

The Commission's fundamental weakness on the budget side is the absence of a long term perspective in financing. This absence is not new, and was already obvious in the october 2001 strategy paper. This is bound to make the conclusion of the enlargement negotiations more difficult, and is also a very bad message for the public opinion, both in the present Member States and in the candidate countries. The effects of this absence are now stronger, since the negotiation covers concrete measures. It is obvious that some things would be more easily imposed in the short term if there are some financial assurances for the middle term.

A new multi-annual financial framework will have to be determined for the period after 2006. As the accession countries will have become members of the Union by then, they will be sitting around the table when the next multi-annual framework is decided. These negotiations will prove very contentious as they will determine the genuine ‘cost of enlargement’.[25] Furthermore, especially if the current economic downturn goes on, a high level of financial solidarity is unlikely. With the prospect of economic recession in Europe, the need to share a finite pot of regional and social funds with the accession countries will distinctly look less attractive to EU voters. Free movement of workers will also look more threatening. All this could potentially boost Euroscepticism.

During the negotiations on the new financial framework, the new member states can be expected to rely heavily on their newly granted political power to undo any accession terms that they feel are unjust and to press for a beneficial deal for themselves[26]. Faced with these demands, the current EU-15 will have a choice between increasing or maintaining the current budgetary guideline. A big increase of the EU’s budget is likely to lead to opposition from the current net contributors. Maintaining the budget at its current level will cause the disenchantment of the current beneficiaries, as they are likely to lose their net benefits, possibly to the point of becoming net contributors. Hence, a discord could emerge between on the one hand the richer members of the EU, pressing for a reduction of their net contributions, and on the other poorer EU-members, asking that their positive net balances be preserved on equity grounds.

Reforms at both the revenue and expenditure side of the budget should be envisaged.

On the revenue side, there are two alternative strategies. The first one is to link in a stronger way budgetary contributions to capacity to pay, i.e. proportional to GDP. The second strategy is on the contrary to reduce the importance of GDP, and develop a new system of own resources. From the institutional point of view, it could be the most adequate approach. It would also reduce the political impact of the debate about "getting one's money back".

On the spending side, the EU policies should be reviewed in order to cater for the preoccupations of net contributors, current net receivers and the new entrants. Both the political and economic benefits of enlargement are unevenly distributed to the detriment of the South European states. As the net contributors stand to gain most from EU enlargement politically (i.e. stability at their borders) and economically[27], there is a case for making them accountable for bearing the budgetary burden of EU enlargement. As a result, an increase in generosity towards the CEECs should come at the expense of CAP expenditure (of which these states are the main beneficiaries) rather than by cutting the Structural Funds transfers[28].

In that way, countries with similar levels of wealth would be treated equally. This would rule out cases like the Danish one: although Denmark is the most prosperous member state after after Luxembourg, it is a net receiver of the EU budget. In

[25] Gros, D., A primer on the cost of enlargement. In: CEPS commentary, Nov. 2001.
[26] There are some precedents from the past, for instance the UK rebate (1984). Baldwin, R., et al., The costs and benefits of eastern enlargement: the impact on the EU and central Europe, Economic Policy, 1997.
[27] See: Breuss, F., Macro-economic effects of EU enlargement for old and new member states. WIFO working paper 143/2001.
[28] Rabinowicz, E., Eastward European Union enlargement and the future of the Common Agricultural Policy. In: Hartell, J., Swinnen, J., Agriculture and East-West-European integration, Ashgate, 2000.

addition, this could 'save' money, which can be used for redistribution purposes. Hence, if one improves the horizontal equity of budget allocations by addressing the current inequitable allocation of budgetary burdens across rich countries, the overall level of redistribution can be maintained or even increased.[29]

During the financing debate, one should not lose out of sight that the EU budget is still rather limited, as it represents just a bit more than 1% of the EU's total GDP. Nor should one forget that net fiscal transfers capture only a (small) part of the benefits of membership of the EU. Furthermore, all evidence suggests that the costs of enlargement for the EU-15 will be clearly outweighed by its political and economic benefits.

Finally, there is also a need for a reflection on whether the current budgetary ceiling should not be increased. The figure of 1.27% of GDP has no economic rationale whatsoever.[30] Given the EMU, it can be argued that more redistribution at the European level should take place to in order to attenuate asymmetric shocks.[31]

3.4. Non discrimination between present and new Member States

All this leads to the most contentious topic of the next years : the principle of non discrimination between present and new Member States. Politically, this is of course essential for the success of the enlargement. A discriminatory treatment towards the new Member States can be justified, provided it respects three conditions. Firstly, it must rely on objective reasons. Secondly, it must be transitory. Thirdly, it must correspond to a long term strategy. It is obvious these conditions are currently not respected by the Commission's propositions.

These propositions are as a matter of fact curiously blind. They do not take into consideration what will happen in the present member states. They do not take into consideration what will happen on the financial side after 2006. This double blindness, both geographical and temporal, looks most unfortunately like the perfect recipe for future problems.

Together, the absence of a sound non-discrimination principle and the blindness of the Commission's proposal are bound to lead to a major political deadlock. The failure to reform the institutional framework of the EU will make it hard to find a way out of the impasse.

[29] De la Fuente, A., Doménech, R., The redistributive effects of the EU budget: an analysis and proposal for reform. In: Journal of Common Market Studies, 2001.
[30] Begg, I., Reshaping the EU budget: yet another missed opportunity. ESRC 'One Europe or several' Policy Paper 1/99.
[31] E.g. De Grauwe, P., The Economics of monetary integration in Europe. Oxford, 1997.