



The Influence of the Economic Crisis on EU Financial Regulations Changes

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ABSTRACT

The occurrence of the global economic crisis has had a widely spread impact on national and European Union economies alike. Reactive measures were taken, on two separate directions: the increase of the fiscal incentives for the private sector (action strongly supported by the USA and Great Britain) or the decrease of public expenditure and the strengthening of financial regulations (viewpoint adopted by the EU). The paper aims to analyze the impact of the economic crisis on the EU budget management (especially for years 2009-2011) and the trends of financial regulations' change foreseen by the European Commission.

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1. Introduction

The world is passing through a severe economic crisis, with global implications, possibly the worst economic downfall after the Great Depression of the 1930's. Due to the interconnections between national economies and supra-national structures, in Europe, the crisis has strongly affected both the national economic sector and the European Union budget. The EU budget has as sources of revenue, among others, national contributions of the Member-States, based on their GNI (almost without exception decreased because of the economic crisis), and a percentage of the Value Added Tax on the sale of products. The decrease of EU revenues was not as much due to a decrease in the amount of national contributions, as due to the severe drop in the trade exchanges. [8]

The anti-crisis measures covered preponderantly two directions: the increase of fiscal incentives granted to the private sector, while maintaining a low level of taxation (point of view vigorously argued by the United States and Great Britain), and the strengthening of fiscal regulations and the decrease of public expenditure as budgetary pressure-relieving instrument (position presented by France and Germany and currently adopted by most EU states). [9] Of course, at the national level, the anti-crisis measures referred to a wide spectrum, with specific national elements.

In the light of the pressures on the EU budget and due to the proven instability of the world financial systems, the European Commission is preparing to issue modifications of the EU financial regulations.

The paper first analyzes the impact of the economic crisis on the European Union budget, presenting a comparative analysis of the budgets for years 2009, 2010 and 2011, in terms of expenditures (respectively, expenditure forecasts for 2011), correlating the figures with the expected budgetary activity for the multi-annual financial period 2007-2013 adopted several years ago. Also, a short analysis is performed on the basis of the 2011 budget amending letters.

Secondly, the paper analyzes the EU agenda of financial regulation, emerged as a consequence of the Commission's proposals and the results of the public consultations of 2009 on the matter.

Although by mid-2010 the European Commission should have made public the report regarding the budgetary activity for the first half of the multi-annual financial period, together with a coherent proposal for the modification of the financial regulations, this has not yet happened. Therefore, we can only speculate on the shaping of the future financial period (2014-2020).

2. EU Budget Amidst and Post-Economic Crisis

When the 2007-2013 multi-annual financial framework was adopted, the economic conditions of the time allowed for its focus on three main directions: sustainable growth (incorporating cohesion and

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competitiveness for growth and employment) and the preservation and management of natural resources; citizenship, freedom, security and justice; and Europe as a global player. [1]

A comparison of the annual budgetary allocations, according to the budgetary expenditure headings, as percentage of the EU budget, is presented in the table below:

Table 1: Comparative budgetary analysis, 2007-2011

Budget heading / Year	2007	2008	2009	2010	2011	2007-2013 average
Cohesion for growth and unemployment	32.9%	31.4%	30.2%	29.5%	32.6%	35.6%
Competitiveness for growth and unemployment	5.5%	8.4%	8.9%	9.2%	9.3%	9%
Preservation and management of natural resources	48%	46.2%	45.3%	47.2%	44.6%	42.5%
Freedom, security and justice	0.2%	0.3%	0.6%	0.6%	0.7%	0.5%
Citizenship	0.7%	0.8%	1.1%	0.5%	0.5%	0.8%
EU as a global player	6.3%	6.3%	6.9%	6.3%	5.8%	5.7%
Administration	5.9%	6.2%	6.5%	6.4%	6.3%	5.8%

Source: Own processing, after data available of the European Commission site.

The flexibility of the budget rules allowed the European Commission to quickly react to the economic crisis, in an attempt to soften the risks faced by countries due to possible long periods of recession. Thus, in late 2008, the European Economic Recovery Plan (EERP) was adopted, diverting part of the EU budget for supporting energy interconnections projects. [2]

Also, the rules regarding financing through the structural and cohesion funds changed drastically, allowing faster payments, simplified eligibility rules and the acceleration of projects' implementation. With the observance of certain conditions, as much as 100% of the financial aid could be paid to beneficiaries, even before the formal acceptance of their projects, while the time intervals necessary for receiving the funds reduced to less than half of the former values. [2]

While the original thought, at the moment May 17th, 2006, date of signing the Inter-Institutional Agreement for the 2007-2013 multi-annual financial framework, provided for 44.6% of the EU budget for sustainable growth, with its two components, of cohesion and, respectively, competitiveness for growth and employment, and 42.5% for the preservation and management of natural resources, the financial allocations actually performed brought about a switch in position of these budget headings, the preservation and management of natural resources accounting for 45-48% of the EU budget, while sustainable growth reached values in the upper 30% (37-39% for the period 2007-2011).

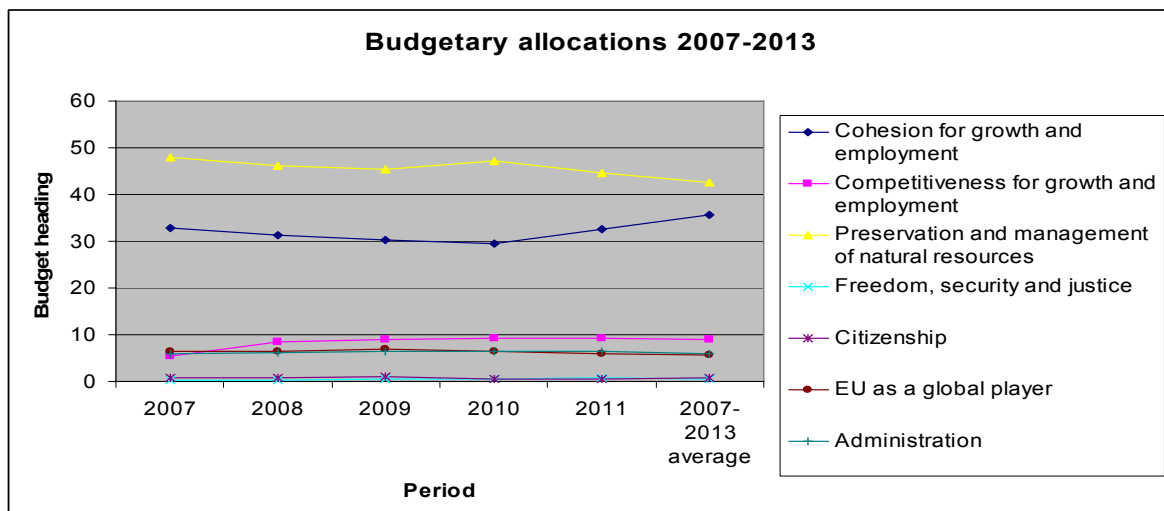


Figure 1. Budgetary allocations for the multi-annual financial period 2007-2013

Source: Own processing, after data available of the European Commission site.

As seen from the figure above, the funding provided by the European Union for the implementation of the energetic projects had an important contribution to the allocation differences between the sustainable growth and the preservation and management of natural resources headings:

However, the draft budget for 2011 foresees an increase by 16.9%, compared to year 2010, for Cohesion for growth and employment, and an increase by almost 7% for Competitiveness for growth and employment. Year 2011 is expected to solidify the economic recovery of the European Union, with the help of actions in line with the Europe 2020 Strategy, aided by financial policies. [8].

The most significant increase of allocation compared to the previous year is foreseen for the areas of freedom, security and justice (12.8%).

The 2011 draft budget adopted in the spring of this year has already suffered modifications. Amending letter no. 1 to the Draft budget for year 2011 refers to the inclusion in the budget of a new section of expenses, namely Section X, comprising the budget appropriations for the European External Action Service (EEAS), established through the Treaty of the EU. [6] This Amending letter does not change the overall value of the EU budget, but advocates in favour of the creation of a separate budget section of the EEAS, which will be financed from money redistributed from the sections regarding the European Council and the European Commission. Thus, the letter suggests the transfer of staff from the Council and Commission to the EEAS, together with the budgetary allocations for those posts. Out of the 1643 positions within EEAS only 118 are new posts (100 requested through draft amending budget 6/2010 and 18 requested through this letter), the rest coming from the Commission (1114 persons) and the Council (411 persons). The document further indicates that the EEAS has to be established according to principles of budgetary neutrality, cost-efficiency and sound financial management, also taking into account the existing economic context.

Amending letter no. 2 to the Draft budget for year 2011 was adopted on October 11th of this year and it refers to an increase of appropriations from the European Union to Europol, to the European Banking Authority (EBA), the European Securities and Market Authority (ESMA), and to the European Insurance and Occupational Pensions Authority (EIOPA). [7] The budgetary impact of Amending letter no. 2 is of 1,776,000 Euros, almost insignificant compared to the overall size of the EU budget.

3. The path to new EU financial regulations

In the light of the economic conditions and considering the unexpected developments of the last years, the European Commission suggested the opportunity of changes of the financial regulations of the European Union, aimed at simplifying the procedures, making the financing process more transparent and allowing greater flexibility and increased reaction speed of the EU institutions before possible future critical events.

Thus, the first step was the elaboration of a questionnaire meant for public consultation, welcoming all contributions of interested parties but specifically targeting the reaction of EU funds beneficiaries, NGO's, private entities and public authorities at all administrative levels (local, regional, national, and European). [8] The public consultation took place between October 19th and December 18th, 2010, and the Commission published the results in May 2010. [8]

The public debate involved 11 questions, in the area of grants (5 questions) and the Commission's handing of financial files (6 questions) and received 235 contributions (107 contributions from organizations, 84 contributions from citizens and 44 contributions from public administration. 30% of total contributions came from multi-national organizations, mostly headquartered in Brussels). According to the importance given by respondents, the questions were grouped as follows:

Major interest: level and quality of information (Q1: Are you sufficiently informed about upcoming calls for proposals in a timely manner? What improvements would you suggest?), flexibility for the co-financing requirement (Q2: Should the rules be more flexible on co-financing requirements taking into account the type of actions and project managers? How could in-kind contributions best be dealt with, while adhering to the non-profit principle?) and simplified grants management (Q3: Should the use of lump sums, flat rates become the norm rather than the exception? Should the rules allow for costs to be covered on the basis of expected outputs? If yes, can you provide concrete examples?). Although the level of information is adequate, the respondents suggested an e-alert system and an annual planning for calls, allowing more time for submitting the applications. Also, different levels of pre-financing were suggested, depending on the project nature.

Great attention: flexibility of the non-profit rule (Q4: Should the rules strictly adhere to the non-profit principle or should there be room for some flexibility in this matter? Do you have examples of good practices from other public authorities?) and improvement of the application procedures (Q11: How could the application procedure for both grants and contracts be further improved?). The contributors stressed the need for an improved application procedure, maybe employing several e-tools, like the electronic signature, and a greater flexibility in applying the non-profit rule.

Large consideration: pre-financing issues (Q8: From your experience, what alternative solutions could be proposed for pre-financing payments while safeguarding taxpayers' money?), matters regarding smaller grants (Q5: What, in your view, would be the appropriate amount for low and very low value grants?), and alternatives to pre-financing guarantees (Q9: What mechanism, other than pre-financing guarantee, could be explored while ensuring adequate protection of community funds?). Most respondents expressed dissatisfaction regarding the pre-financing payments and suggested the making of the cost of a bank guarantee eligible for reimbursement by the EU.

The other issues subjected for public consultation (Q6: How could the rule on operating grants be more flexible? In which way? What are your views on the duration of framework partnership agreements? Q7: Can you give concrete examples and types of actions where the strict limitation on cascading grants became an

obstacle for achieving the goal of your action? Q10: Based on your experience, do you think the current thresholds are still adequate or they should be increased, and why?) did not grasp the attention of most contributors. Also, the responses varied very much, for example the proposed period for partnerships ranging between three and seven years.

Romania contributed to the public consultation with two documents, one elaborated by the Bucharest Municipality (P011 - sent on 12/15/2009) and one drafted by the Romanian Municipalities Association (RMA) (P036 - sent on 12/18/2009). [8] The Bucharest Municipality mainly referred to grant awarding, emphasizing the difficulties faced by public administration in providing co-financing, and suggesting the possibility to contribute in kind. The Romanian Municipalities Association brought attention to the language barrier, considering that the calls for proposals are usually elaborated in English and to the need of using more ITC tools. Finally, the RMA suggested the introduction of the EU label of "good applicants" who would benefit of a reduced paper-load when applying for future grants.

4. Conclusions

The global economic crisis has changed the approach of the European Commission to the financial regulation. The need for flexible rules, for quick transfers of money and for the implementation of transnational projects is very evident now.

After public consultation and feedback from the economy, the main issues of the European Commission agenda in matters of financial regulations are [9]:

a) Regulating capital markets and market actors. In its 'safety-first' approach, the EC fills the gaps left by insufficient or incomplete national financial regulations. The topics addressed range from tighter financial markets regulations to future avoidance of taxpayers carrying the burden of banks bailouts; from tighter controls on credit rating agencies, increase of transparency and financial stability at the EU level to the obligation of insurers to match their capital more adequately with the risks registered in their books. [9]

As a result of these proposals, in September 2010 was adopted the European financial supervision package, consisting of two elements: the creation of the European Systemic Risk Board (ESRB) to safeguard the stability of the financial system; and the creation of other three supervisory agencies, for the overall supervision of banks (European Banking Authority - EBA), securities and market (European Securities and Market Authority - ESMA), and insurance and occupational pensions (European Insurance and Occupational Pensions Authority - EIOPA). The agencies will start their work in January 2011, with financial means provided through Amending letter no. 2 to the Draft budget 2011, discusses previously.

b) Retail financial products. The Commission aims to strengthen the protection of the investor and the financial consumer and to support legislation on responsible lending and borrowing, as well as with respect to the credit history.

c) Sanctions for market abusers. The Market Abuse Directive is expected to come into effect on December 8th, 2010, hardening the sanctions for violations EU legislation in the financial realm.

d) Insurance. The suggested modification refers to the introduction of the risk-based approach regarding capital requirements of insurers (Solvency II Directive).

It must be mentioned that although the European Commission offered EU citizens, enterprises and public administrations the opportunity to express their thoughts on the financial regulations, the period for public consultations was rather short, of only two months. At the same time, given the huge impact of financial regulations on accessing EU funds and on implementing projects, the number of contributions (235) seems completely inadequate and insignificant. If we add that 84 contributions came from private persons, the picture is even more puzzling. The level of public participation and involvement in European Union common interest issues is very low, and, in order to achieve greater efficiency, I believe the need arises for greater solidarity and a higher sense of belonging.

Brought about by the unfortunate economic crisis, the future financial regulations of the European Union may prove to be useful tools for economic development, but they must work in line with an increase of social cohesion and social capital.

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