The Next Generation EU Recovery Fund & MFF 2021-2027 – European Council Summit Agreement

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EU Service Team

Executive Summary

- Following debatably the longest summit in the European Council's history, EU leaders agreed upon a draft of the Next Generation EU (NGEU) COVID-19 Recovery Plan, as well as the 2021-2027 Multiannual Financial Framework (MFF).
- The NGEU will remain worth €750bn as proposed in May 2020 but will now be composed of grants worth €390bn and loans worth €360bn. Initially this ratio was to be €500bn/€250bn.
- Member States will be required to submit their recovery and resilience plans for assessment to the European Commission, and there is a mechanism to freeze payments where there is "serious deviation".
- The MFF has slightly decreased from the May 2020 proposal of €1.1tn to €1.07tn.
- Notable reductions to the MFF include a 56% funding reduction to the Just Transition Fund, a core pillar of the European Green Deal.
- Reductions have also been applied to InvestEU, health, migration and external action programmes.
- The key debates which will now arise in negotiations with the European Parliament include governance of the unprecedented NGEU package, the status of rebates and the conditionality of rule of law guarantees on accessing funds.
- President Sassoli will meet European Parliament group leaders on 22 July, and there will be a meeting of the European Parliament plenary on 23 July to offer an initial assessment of the MFF.
- The Council expected to vote on the Own Resources Decision in autumn 2020 following a consultation procedure with the EP.
- The final stages of budgetary ratification will be ratification by national parliaments and the General Affairs Council by the end of 2020.
- The current 2014-2020 MFF expires after 31 December 2020.

The Recovery Plan

Attached to the Multiannual Financial Framework (MFF) 2021-2027 is the Next Generation EU package. This is the Union's COVID-19 recovery fund. EU leaders have agreed a budget of €750bn - €390bn of which will be made up of grants, and the remaining €360bn in loans.

In the Council's agreement, the Recovery and Resilience Facility (RRF) fund represents the largest single budget within NGEU. It is hoped this programme will help strengthen Member State economies through supporting improvements in competitiveness, productivity, environmental sustainability, education and skills, health, employment, and economic, social and territorial cohesion.

However, the €112.5bn increase in the RRF budget since the initial European Commission proposal in May 2020 has been at the expense of all other NGEU programmes. They have seen finance earmarked for them either slashed or excluded completely in the case of the Solvency Support Instrument, the Health Programme, and the Neighbourhood, Development and International Cooperation Instrument (NDICI).

While the overall €750bn figure remains consistent with the Commission proposal, the final agreement represents a significant reduction (€110bn) in the proportion of the recovery fund that is made up of grants. Indeed, France, Germany, and in turn the Commission, favoured a €500bn grant package.

However, it is likely that those in favour of grants within the Council will take greater comfort from the final agreement. After all, prior to the summit the Netherlands and Austria had been vocal in their opposition to the inclusion of grants within the recovery plan altogether.

The mutualisation of debt in order to finance the recovery fund is a historic step for the EU and will make it easier to take on further debt in the future. The markets reacted immediately. Germany's DAX rose to five-month highs and the euro to a four-month high while Italy's borrowing costs fell to their lowest since early March. If implemented properly, the mutualisation will mean a stronger euro and real European solidarity as one single signature will be enough for common bonds.

Member States will be required to submit their recovery and resilience plans for assessment to the European Commission. These plans should be based on the European semester recommendations. Their contribution to the green and digital transition will also be a key requisite for a positive judgement. Crucially, the plans will require qualified majority support in the Council.

In the event that a Member State is suspected of a 'serious deviation' from their proposed recovery plan, there is a mechanism to temporarily freeze payments.

The process is as follows: after the initial implementation by Member States, the plans will be expected to satisfy the fulfilment of relevant milestones and targets. A positive assessment will require unanimity within the Economic and Financial Committee. In the case that one or more Member State raises concerns about the implementation, it shall be raised at the next European Council meeting. In the meantime, recovery assistance can be frozen for up to three months.

The European Commission will have the final decision on whether to approve further payments.

May 2020 – July 2020 Comparison between NGEU following Summit

Programme	**May 2020**	**July 2020**	**Change**
Recovery and Resilience Facility	€560bn	€672.5bn	+€112.5 bn
ReactEU	€50bn	€47.5bn	-€2.5 bn
Horizon Europe	€13.5bn	€5bn	-€8.5 bn
InvestEU	€30.3bn	€5.6bn	-€24.7 bn
Solvency Support Instrument	€26bn	Nil	-€26bn
Rural Development	€15bn	€7.5bn	-€7.5bn
Just Transition Fund (JTF)	€30bn	€10bn	-€20bn
RescEU	€2bn	€1.9bn	-€0.1bn
Health Programme	€7.7bn	Nil	-€7.7bn
Neighbourhood, Development and International Cooperation Instrument (NDICI)	€15.5 bn	Nil	-€15.5bn
Total	**€750bn**	**€750bn**	**nil**

The Multiannual Financial Framework 2021- 2027

The overall amount of the MFF has been slightly decreased from €1.1trn as of May 2020 to €1.07trn in the current agreement, only the commitment made to the area of Cohesion, Resilience and Values has increased in size. €5bn will be allocated to special instruments to counter unforeseen and adverse consequences in Member States and sectors that are worst affected.

The annual appropriations for payments is fixed at 1.4% of the GNI of all Member States and the total annual amount of appropriations for commitments shall not exceed 1.46% of the sum of GNI of all Member States. A drain on future EU budgets will be the establishment of a yield curve of debt issuance which includes all liabilities to be repaid by the end of 2058. The EU will work towards introducing new own resources, which may include a Financial Transaction Tax. These new proceeds will be used to repay the NGEU borrowing. The existing rebates for the Netherlands, Austria, Denmark, and Sweden were increased while Germany's stayed the same.

The Council emphasised the importance of the protection of the Union's financial interests as well as the importance of the respect of the rule of law as a condition to receive money from the Recovery Fund and the MFF. The European Parliament especially requested to make the contributions dependent on the respect of the rule of law, which was threatened with a veto by Hungary and Poland.

While the original proposal would have allowed to trigger the conditionality mechanism unless a qualified majority of governments would have blocked it, Euronews reported that the current proposal works the other way around, requiring a qualified majority of governments to trigger the mechanism, which means 15 countries with at least 65% of the population of the EU. The Council still has to agree to this Regulation, allowing for this, which it has been working on since May 2018.

May 2020 – July 2020 Comparison between the 2021-2027 MFF

Heading	May 2020	July 2020	Change
Single Market, Innovation and Digital	€140.7bn	€132.8bn	-€7.9bn
Cohesion, Resilience and Values	€374.5bn	€377.8bn (€330.2m for Economics, social and territorial cohesion)	+€3.3bn
Natural Resources and Environment	€357bn	€356.4bn (€258.6 for market related expenditure and direct payments)	-€0.6bn
Migration and Border Management	€31.1bn	€22.7bn	-€7.4bn
Security and Defence	€19.4bn	€13.2bn	-€6.2bn
Neighbourhood and the World	€102.7bn	€98.4bn	-€4.3bn
European Public Administration	€74.6bn	€73.1bn (€55.9 for administrative expenditure of the institutions)	-€1.5bn

MFF 2021-2027 Sector Analysis

Transport, Energy & the European Green Deal

There were a number of headlines relating to the European Green Deal, and more specifically the short and longer term of EU transport and energy policy.

Those supporting the deal's green credentials will cite a climate funding target of 30% of MFF and NGEU spending which will apply.

Another major step forward in the story of the European Green Deal and the fresh MFF and NGEU proposal relates to the EU's Carbon Border Adjustment Mechanism as a new own resource solution. For the first time, the EU has committed to bringing forward proposals by the first semester of 2021 with a view towards implementation in January 2023.

Member States also redoubled a commitment to bulk up income from the ETS, stating a "possible" extension to aviation and maritime. Another positive development for those in transport is a significant increase in funding for the Connecting Europe Facility. The pot for energy projects has, though, been slightly reduced.

There are likely to be major questions asked by the European Parliament on what has been described by some as a "gutting" of the Just Transition Fund. The JTF which is currently moving through the European Parliament has suffered a 56% overall funding cut, with its grants being decreased by two thirds.

Health

As the COVID-19 constitutes a health crisis, the Commission has proposed in May a standalone EU4Health programme of €7.7bn to address the impact of the crisis. Additional funding would have been available from the rescEU initiative, aiming at making the EU resilient in future crises.

Despite the fact that the rescEU has seen only a minor reduction in its budget, it seems that the EU4Health programme has been diminished substantially with no specific reference mentioned. However, a new health programme will be established with a budget of €1.7bn, a number to be highly debated concerning its effectiveness in providing aid to the healthcare and pharmaceutical sector.

Rural Development & External Action

On rural development, last minute increases provided for the budget for rural development made the allocation for European Agricultural Fund for Rural Development stand at €77.85 bn. The allocations to France, Finland, Germany and Slovenia grew since Michel's Saturday night budget proposal recognising once again the power of the agricultural sector in the EU.

On the external action, the EU's initiatives for the rest of the world were also affected by the cuts. The proposal includes €70.8bn for the Neighbourhood, Development and International Cooperation Instrument (NDICI), suffering a cut of €15bn. The funding represents a 3.15% reduction compared to current financing levels pre COVID-19 and excluding UK contributions.

Research and Innovation

Over the past few months, there has been much talk of Europe becoming a powerhouse in research and development. Only last week, Commissioner Breton argued that Europe could one day lead the global technological race. However, the 'Frugal Four's' desire for a smaller MFF has been at the expense of R&I .

Horizon Europe, the EU's flagship R&I programme, will receive a budget of €75.9bn between 2021 and 2027. This is a significant reduction from the European Commission's initial May 2020 proposal which earmarked €98.775bn. In comparison, the previous MFF's Horizon budget was c. €79bn.

Meanwhile, the Digital Europe programme will receive €6.761 bn. The Commission had proposed €8.2bn. The digital budget of the Connecting Europe Facility has also seen a reduction from its May 2020 level.

Key Debates & Next Steps

The MFF and Recovery Fund proposal adopted by the European leaders has changed from the European Commission's initial proposal on May 2020, with President Ursula von der Leyen expressing her disappointment that the leaders have agreed on reduced funding for important aspects of the proposal such as in InvestEU, health, migration and external action.

These changes will come under scrutiny from the European Parliament, which in its position has underlined that new own resources and a robust MFF is essential. In an initial comment, the EP negotiators welcomed the effort but criticised parts of the agreement concerning funding cuts, governance of the Recovery Instrument and the respect for the rule of law.

Key Debates

R&D Programmes

The EP position has stated that its intention is to boost the EU's flagship programmes in the field of research, innovation, digital and environment.

· The final Council-adopted version which foresees cuts in the fields of Horizon Europe, the InvestEU initiative and the Just Transition Fund is expected to be criticised by the MEPs, especially the Greens/EFA Group. Going even further, the EP negotiators have warned that if their conditions on the MFF programmes are not met, they will adopt the programmes on the basis of the existing budget.

The Council's position is also going against the European Commission's narrative that the priorities of the EU recovery from COVID-19 is going to focus on green and digital initiatives.

Rule of law

The much-debated rule of law conditionality has been watered down in the final agreement in favour of a few MS, reading that *"the European Council underlines the importance of the respect of the rule of law".* The line on further measures to be proposed in case of breaches of the rule of law seems as vague and goes against the EP's proposal for the creation of a new mechanism to protect the EU budget where the rule of law is not respected.

Own resources

The EP's position indicates the importance of the financing of the MFF to take place under a system of own resources as of 2021 and noted that its consent is conditional on the introduction of such a basket.

From this pool the Council agreement only proposes that a new own resource based on non-recycled plastic waste will be introduced and apply as of 1 January 2021 and it will look for further options to be introduced no earlier than 2023.

However, the likelihood of those new charges getting unanimous backing is unlikely.

Governance

The final proposal has undermined the role of the Parliament in the governance and the implementation in particular of the Recovery and Resilience Facility. The national recovery plans will be assessed by the Commission and approved by the Council through an implementing act and an opinion of the Economic and Financial Committee. No reference to the EP included in the process is made.

Rebates

Regarding rebates, the EP is strongly opposing rebates which under the final proposal are increased and not abolished.

Next steps

Today's agreement between the EU leaders constitutes the European Council's common position in the negotiations with the European Parliament, as the budgetary procedure requires the Parliament's consent. In these discussions, the EP will be represented by its negotiating team and its President David Sassoli.

In that context, the EP President announced an extraordinary plenary session on Thursday morning 23 July in order for MEPs to conclude an initial assessment of the European Council conclusions and publish their own resolution. Ahead of the plenary session, President Sassoli will meet the political group leaders on Wednesday to frame the direction of the debate.

Negotiations are going to continue throughout autumn and the Parliament has to give its consent by the end of 2020, so that the Council can approve the political agreement reached by both Institutions before 2021, in order for its implementation to begin swiftly.

The Council is under pressure to secure the European Parliament's consent, and a failure to do so could easily create major problems with spending instruments which are due to expire at the end of 2020. In order for the European Parliament to ratify the MFF, an absolute majority of MEPs is required to secure Parliament's consent.

Finally, on the Own Resources Decision, the Council is expected to vote in autumn 2020 following a consultation procedure with the EP. Once it has been adopted, Member States' national parliaments will proceed with its approval as soon as possible.

It remains to be seen whether the EP will adhere to its positions concerning a higher MFF, a strong rule of law mechanism and more investment in research and development programmes thus delaying the MFF adoption.