



What to expect from the EU in 2011

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1. What's next for the eurozone?

The eurozone is set to face massive challenges in 2011. Between them eurozone governments have to raise €560 billion next year according to UniCredit – the highest amount since the introduction of the euro.¹ In addition, banks in the eurozone face re-financing targets of €1.3 trillion over the next two years.²

Estimates vary as to how much individual governments have to raise. According to credit rating agency Moody's, Spain has to raise €170bn next year, with regional governments having to find another €30bn. At the same time, the country's banks will have to raise €90bn. Moody's has threatened to downgrade Spanish debt another notch over fears that the country will face difficulties in meeting these targets.

One of the more acute problems with Spanish banks is that their potential exposure to bad loans remains unclear, which is creating huge uncertainty as to the true state of the Spanish economy. Should Spanish banks, including the country's small savings banks, the *cajas*, continue to suffer losses on sub-prime loans, things could get out of control very quickly and therefore Spain clearly remains the eurozone's biggest worry going into 2011.

EU leaders have agreed to a permanent eurozone bailout fund in principle but this will not come into effect before 2013. Meanwhile, Italy has to raise some €192bn next year, while Portugal has to raise €15-20bn. With Ireland and Greece already on life support from the EU and the IMF, the question is, will Portugal, Spain, Italy and even Belgium be able to service their national debts next year? And what happens if they fail to do so?

Will EU leaders be forced to put more bail-out cash on the table?

EU leaders may well be faced with this question very early in the New Year, with debt maturity deadlines looming large. Doubts exist in the markets and among some governments as to whether the current bail-out package is big enough to rescue Spain and Portugal, in addition to Greece and Ireland all at once.

On paper, the EU/IMF bail-out package is currently worth €750 billion in total (€250 billion of which coming from the IMF). However, the real amount available is something closer to €409 billion after taking into account the countries that themselves are already on support and the need for the European Financial Stability Facility (EFSF) to retain a 'Triple A' credit rating.³

¹ "Euro crisis fears grow amid debt moves", 12 December 2010, <http://www.ft.com/cms/s/0/f9d781f6-0619-11e0-976b-00144feabdc0.html#axzz18kUKuu00>

² ECB Vice-President Victor Constancio quoted in <http://www.lesechos.fr/entreprises-secteurs/finance-marches/actu/020993776009.htm>. See also the most recent ECB Financial Stability Review (graph on page 88), here <http://www.ecb.int/pub/pdf/other/financialstabilityreview201012en.pdf?e5e7752e6f2c57487e204de02161e00d>

³ There are several different ways in which the true size of the bail-out package can be calculated. First, the contributions from Greece and Ireland have to be subtracted (€19 bn between them) from the original €440bn EFSF, as they themselves are receiving aid and are therefore exempt from contributing. Secondly, to ensure a 'triple A' credit rating – and therefore low borrowing costs – eurozone governments are guaranteeing 120 percent of each bond raised (allowing for a reserve that can never be used). In addition, as S&P-Analyst Moritz Krämer has pointed out, the share of eurozone governments without a triple A rating must also be discounted, if the triple A rating of the EFSF is to be guaranteed. This means that the real size of the EFSF is €213 billion, with another €60 billion added through the European Stabilisation Fund. Importantly, under the agreement struck in May, the IMF

This should be weighed against the potential cost of bailing out several eurozone economies. According to a Goldman Sachs estimate, taking Ireland, Portugal and Spain out of the bond markets for two years will cost €450 billion.⁴ Others put the figure higher, with Cornelia Meyer, CEO at MRL Corporation, predicting that a Spanish bailout alone is likely to cost up to €500 billion.⁵

Given how fragile the situation in the eurozone is, any more jitters on the markets early in the New Year could force EU leaders to substantially increase the size of the existing bail-out package. This, in turn, is likely to trigger new objections from within member states as taxpayers in the richer countries face ever-higher costs for the mistakes of foreign governments that they cannot vote from office.

Alternatively, the mandate of the EFSF could be expanded to allow it to purchase eurozone government bonds in an effort to narrow bond yields and reduce borrowing costs for struggling economies. However, that would require new, complicated negotiations as the current EFSF agreement prohibits such a strategy⁶. So far, this move has been resisted by Germany.

Will countries be forced to restructure their debts in 2011?

An increasing number of observers now see a restructuring of eurozone debt as a likely possibility. A recent survey of investors, including hedge funds and propriety traders, conducted by Barclay's capital,⁷ showed that one in three investors is expecting at least one eurozone country to default on or restructure its debt in 2011.

Almost 60% expect further bail-outs by the EU or IMF. Investors favouring a short position on Spanish and Italian sovereign debt outnumbered those who recommended a long position by two to one, though only 4% thought that the eurozone would break up.

Will electorates and parliaments agree to more austerity?

2011 will also see continuing protests aimed at the various austerity measures pushed through by governments across the eurozone. A huge test will come in Ireland, which will hold a general election, most likely in February or March 2011. Fianna Fáil is likely to be heavily punished over the government's handling of the economy, the banks and the EU/IMF bail-out.

Fine Gael and Labour – the two main opposition parties – have both criticised the €85 billion EU-IMF bailout package the country was forced to accept in November, calling it “unfair” and a “sell-out”. During the debate on the package in the Irish Parliament, the Dáil, which saw the deal pass with only a six vote majority, Fine Gael Finance Spokesman Michael Noonan said, “The Government's negotiations have led to a very bad deal. The deal needs to be re-negotiated and Fine Gael will look for a mandate to do so.”⁸

would only add 50 percent of the sum the EU provides, meaning €136 billion as opposed to the original €250 billion, leaving a total of €409 billion.

⁴ Cited in <http://ftalphaville.ft.com/blog/2010/12/10/433426/what-a-difference-an-efsf-year-makes/>

⁵ Cited in <http://www.openeurope.org.uk/media-centre/summary.aspx?id=1242>

⁶ *iMarketNews*, ‘Germany's Govt: Oppose Idea Of EFSF Buying Up EMU Govt Bonds’, 13 December 2010; <http://imarketnews.com/node/23845>

⁷ *FTfm*, “One in three institutional investors expect a eurozone default” 21 December 2010, <http://www.ft.com/cms/s/0/94c0b864-0b64-11e0-a313-00144feabdc0.html#axzz18dzclVMH>

⁸ *Irish Times*, “Dáil approves bailout deal”, 15 December 2010, <http://www.irishtimes.com/newspaper/breaking/2010/1215/breaking1.html>

The big uncertainty is therefore whether a new Irish government would seek re-negotiations over better terms and interest rates from the IMF and the EU, and whether it would also look to back-track on some of the commitments to cut public spending. Voters would be within their rights to demand this but such moves would also undoubtedly lead to instability on the markets.

The IMF and European Commission will put huge pressure on the new Irish government to stick to the terms. IMF boss Dominique Strauss-Kahn has said, "They'll stick with the program....I'm confident they won't question in any way the global framework of this program."⁹ And before the adoption of the Irish budget, EU Commissioner for Economic and Monetary Affairs, Olli Rehn, said that he did not "have a position on the domestic democratic politics of Ireland", but added that "The budget needs to be adopted. Ireland will pass the budget in the time foreseen and certainly sooner than later. Let's get it out of the way and let's move on."¹⁰

This clash between national politics and the external demands of the unelected IMF and EU institutions is likely to become more stark as austerity continues to bite, illustrating the democratic deficit now present in the eurozone. Besides the Irish general election, Portugal will hold presidential elections in 2011 and outbursts against austerity will continue in countries such as Spain and Greece.

Will German taxpayers agree to more bail-outs?

Regional German elections in Baden-Württemberg, currently a stronghold for Chancellor Angela Merkel's CDU party, on 27 March 2011 are seen as a huge test of her response to the euro crisis¹¹. This year the CDU dropped¹² by more than 10 points in regional elections in Germany's most populous state, North Rhine-Westphalia, following the announcement of the €110 Greek bailout. The Baden-Württemberg elections will be the first major test in the CDU's heartlands after the 'shock and awe' €750bn bailout fund was agreed. Polls so far indicate around 5% losses for both the CDU and their coalition partners the FDP¹³.

So far German politicians seem willing to test their voters' willingness to foot the bill for euro bail-outs to the limit.

Will the EU and eurozone agree on an economic government?

The development of 'economic governance' by the EU and the eurozone in particular is both an attempt to avoid future crises and set out the conditions for countries receiving EU help.

Monitoring national budgets

⁹ Reuters, "IMF chief says Ireland will keep IMF-EU program", 16 December 2010, <http://www.reuters.com/article/idUSN166175520101216>

¹⁰ Irish Times, "Ireland 'must pass budget soon'", 23 November 2010, <http://www.irishtimes.com/newspaper/breaking/2010/1123/breaking17.html>

¹¹ Spiegel, 'Could State Election Spell End for Merkel?', 13 October 2010; <http://www.spiegel.de/international/germany/0,1518,722997,00.html>

¹² Business Week, "Merkel's CDU Gets Worst Postwar Result on Greece", 10 May 2010, <http://www.businessweek.com/news/2010-05-10/merkel-s-cdu-gets-worst-postwar-result-on-greece-update2-.html>

¹³ 10 polls are being cited on the Wikipedia page of the upcoming election http://de.wikipedia.org/wiki/Landtagswahl_in_Baden-W%C3%BCrtemberg_2011

2011 will see the implementation of the 'European semester' under which national governments will have to submit their budgets both to the Commission, and to other national finance ministers for peer review, before they are approved by national parliaments.¹⁴ The details remain vague but key budgetary information such as total revenues, total spending and deficit targets are likely to be included.

The UK will submit its pre-Budget report for peer review but will be exempt from any binding sanctions or recommendations agreed by eurozone members.

Economic sanctions for eurozone countries breaking the rules?

EU Council President Herman Van Rompuy and the Commission are proposing economic sanctions for eurozone countries that not only break the EU's debt and deficit rules but also for countries that fail to act on recommendations to address wider macroeconomic imbalances, such as on labour costs or a build-up of private debt¹⁵. Van Rompuy has said eurozone governments could be fined as much as 0.5% of GDP¹⁶. There continue to be disagreements about how strictly the sanctions would be enforced¹⁷.

This is an attempt to address the diverging competitiveness within the eurozone. However, the fact remains that, under one interest rate and without the option of devaluation, little can be done by uncompetitive countries except to depress their costs at home (such as labour costs) over a sustained period. There is little appetite for this extent of austerity on the eurozone periphery.

Questions remain over how much influence Chancellor Angela Merkel will have on the economic governance proposals. Germany's strong exporting position has been built on its competitiveness and low costs and it will firmly resist any attempts to water down those advantages, even in the spirit of 'EU solidarity'.

What shape will a permanent eurozone bailout fund take?

At December's European Council summit, EU leaders agreed on a treaty change to establish a permanent eurozone bail-out fund post-2013, which would include investors taking losses in future bailouts. The size and scope of the new bail-out mechanism is still unclear, with the details expected to be decided throughout 2011 – following tough behind the scenes negotiations. EU leaders have stated that the amendment to the EU treaty needs to enter into force on 1 January 2013. The European Council summit of 24-25 March will aim to formally adopt this amendment.¹⁸

¹⁴ The European has noted that for this "Immediate legislative changes do not appear to be necessary", see: European Commission Communication COM(2010) 367/2, "Enhancing economic policy coordination for stability, growth and jobs – Tools for stronger EU economic governance", http://ec.europa.eu/economy_finance/articles/euro/documents/com_2010_367_en.pdf

¹⁵ European Commission press release, "A new EU economic governance - a comprehensive Commission package of proposals", 29 September 2010 http://ec.europa.eu/economy_finance/articles/eu_economic_situation/2010-09-eu_economic_governance_proposals_en.htm

¹⁶ Bloomberg, "European Nations Violating Deficit Caps May Face Fines Up to 0.5% of GDP", 19 Dec 2010 <http://www.bloomberg.com/news/2010-12-19/european-nations-violating-deficit-caps-may-faces-fines-up-to-0-5-of-gdp.html> and Buitenhof TV program in Dutch, 26'20 minutes in, 19 Dec 2010 <http://www.vpro.nl/programma/buitenhof/afleveringen/44024909/media/44302962/?bw=bb&player=wmp&media=44302962&referr=&hostname=www&portalid=programmasites&x=37&y=10>

¹⁷ FT Editorial, "The fiscal future of the eurozone", 20 Dec 2010 <http://www.ft.com/cms/s/0/c3b3e4d6-0c75-11e0-8408-00144feabdc0.html#ixzz18rAEjiH8>

¹⁸ European Council Conclusions 16-17 December 2010 http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/118578.pdf

The new arrangement will go under the name the “European Stability Mechanism” (ESM) and will replace the current emergency bailout funds, which will remain in force until June 2013. David Cameron has confirmed that the UK will remain liable for future eurozone bailouts until 2013, under its share of the existing €60bn European Financial Stability Mechanism – whose activation, crucially, is decided by majority voting.

Nothing has yet been agreed about how big a permanent bailout fund will be, but a German diplomat was quoted following December’s summit saying, “If you have a permanent mechanism then it cannot be limited. A permanent crisis mechanism has to be unlimited in its size.”¹⁹

The most significant innovation is the proposed incorporation of “collective action clauses” in all eurozone government bonds issued after June 2013, whereby creditors will have to agree on terms for debt restructuring by qualified majority voting.²⁰ EU leaders have a daunting task in trying to decide how this proposal will work in practice and huge uncertainties remain. For example, how strict can the conditions imposed on lending countries realistically be? Will the new debt issued with collective action clauses be cheaper than the existing stock of debt and what will that mean for the markets?

Will the EU produce robust stress tests for banks?

Any situation that the eurozone will find itself in 2011 will very much come down to the state of Europe’s banks – on the individual as well as systemic level.²¹ For example, the most recent quarterly data published by the Bank of International Settlements shows that European banks have a €656.6bn total exposure to public and private debt in Spain – which shows why a Spanish meltdown would be so disastrous.²² And as noted above, the state of Spanish banks themselves is not clear at all.

It is clear that the EU needs to conduct a series of robust, non-politicised stress tests of the region’s banks in order to identify their true financial positions and likely losses – and try to minimise risks accordingly. Off the back of such tests there needs to be a serious discussion about whether some banks – that clearly are insolvent – should continue to receive support, or whether a sustainable solution is to wind some of them down. The Commission has already pushed Irish banks to transfer some losses to investors as a condition for approving a deal which saw the Irish government pump in another €17.5bn into Anglo Irish Bank, AIB and Irish Nationwide.²³ It will be interesting to see how strongly the Commission will push this line in 2011.

However, there will be major questions marks against the rigour of the second round of stress tests, due to be carried out in February. Stress tests carried out last year gave Irish banks a clean bill of health only for the same banks to bring down the entire country a few months later. Germany is opposing ECB and European

¹⁹ Die Welt, “Merkel setzt Auflagen für Pleiteländer durch”, 17 Dec 2010

<http://www.welt.de/politik/ausland/article11677054/Merkel-setzt-Auflagen-fuer-Pleitelaeender-durch.html>

²⁰ European Council Conclusions 16-17 December 2010, page 10,

http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/118578.pdf

²¹ For example in our briefing on the Irish bailout, page

12: <http://www.openeurope.org.uk/research/irelandbailout.pdf>

²² FT, Bank exposure: the Eurozone risk”, 1 Dec 2010 <http://www.ft.com/cms/s/0/9686c004-fca4-11df-bfdd-00144feab49a.html#axzz18rhmmj9E>

²³ Irish Independent, “EC agrees €17.5bn banks injection”, 22 December 2010,

<http://www.independent.ie/business/irish/ec-agrees-euro175bn-banks-injection-2470020.html>

Commission proposals to include a clear liquidity criterion in the new round, fearing a run on the country's fragile regional banks, the *Landesbanken*.²⁴ Detailed criteria for the tests are to be agreed in January.

Closer Franco-German cooperation on economic and fiscal policy

President Nicolas Sarkozy and Chancellor Angela Merkel have announced they will propose plans early next year for greater harmonisation of tax and labour policies within the eurozone. It is "important that we have a common economic policy," Merkel said²⁵.

2. The future of the EU budget

2010 saw turbulent negotiations on next year's annual budget, which resulted in an increase of 2.9%. However, 2011 will see attention shift to the vastly more important multi-annual EU budget, which will run from 2014 for between five and ten years but probably up to 2020. National governments have a veto over these key negotiations that will decide the size of the EU's long-term spending. For example, how much funding is allocated to the EU's wasteful farming subsidies versus research and development. The Commission must present its proposals for the size and shape of the budget by 1 July 2011. Once the Commission tables its proposals, governments will start the familiar process of horse-trading.

The negotiations will be driven by two key fault-lines. Firstly, between the countries which pay in to the EU budget (net contributors), who will seek to limit or reduce the budget, and those which benefit (net recipients), who will argue for increases. And secondly, between reformers, who want to see more EU money invested in innovation and growth, and those keen to maintain the status quo, which will resist moves to dismantle the EU's two outdated subsidy streams, the Common Agricultural Policy (CAP) and the Structural Funds that currently account for 42% and 35% of the entire budget.

In addition, the Commission and the European Parliament (that have co-decision powers over the budget under the Lisbon Treaty) clearly side with the countries that want big increases to the budget. The EP has also consistently sought to block reform to the CAP, so its strengthened position under Lisbon has made reform of the EU's flawed farm subsidy scheme even more difficult.

The UK will be a key player in determining future of EU budget

Against the backdrop of national spending cuts, David Cameron has already made it clear that his priority is to seek a freeze on long-term EU spending or at least a deal that would reflect changes to national government expenditure. At December's European Council meeting he circulated a letter, backed by France, Germany, the Netherlands and Finland, demanding that,

"European public spending cannot be exempt from the considerable efforts made by the member states to bring their public spending under control.

²⁴ Reuters, "ECB wants liquidity included in new stress tests: sources", 20 Dec 2010
<http://www.reuters.com/article/idUSTRE6BJ2PI20101220>

²⁵ FTD, "'Berlin werkelt an einem neuen Europa", 22 December 2010

*Payment appropriations should increase, at most, by no more than inflation over the next [2014-2020] financial perspective*²⁶.

Swedish Prime Minister Fredrik Reinfeldt has criticised the letter arguing that it could, in fact, leave the possibility of a budget increase. He said,

“We see it as a bit ambiguous and from a Swedish point of view, not restrictive enough when it comes to the budget...our position is that even the possibility of increasing the budget that the signatory countries are open to is too far-reaching.”

Reinfeldt also made the point that Cameron’s approach may have the effect of closing down any reform of *how* EU money is spent. “First we want to discuss the content in the budget, what we should spend the money on. When that is done, we can see what it costs.”²⁷

The UK and France, more than any others, hold the key to the future of the EU budget. Without a break in the stalemate between French defence of the CAP and Britain’s defence of its rebate, there is very little possibility of significant reform or modernisation. However, it seems unlikely that there will be much progress, with diplomats revealing that, “Sarkozy said that if Cameron leaves farm subsidies alone, then he, in turn, would leave the British rebate alone.” The UK Government has denied a deal has been done and these are still early days in the negotiations.²⁸

Tony Blair rightly came under severe criticism for giving up a sizeable chunk of the UK’s rebate in the last round of EU negotiations in 2005 precisely because there was no reciprocal change to the CAP. But defending the rebate at all costs risks holding any meaningful reform of the budget to ransom. The UK should instead be prepared to listen to offers for any reduction in the rebate but only if they are lasting and tangible.

EU taxes?

As a “sweetener” to MEPs for agreeing the 2011 budget, the Commission has promised to draw up a proposal for the introduction of EU taxes post-2013. This will be presented along with the Commission’s other proposals on the budget before June 2011. One or more of the following options is likely to be proposed by the Commission: a share of a financial transaction or financial activities tax, auctioning of green house gas emission allowances, an EU charge related to air transport, a separate EU VAT rate, a share of an EU energy tax or of an EU corporate income tax.²⁹

National governments, including the UK, France and Germany, have all rejected the idea but this has done little to quell the long-standing ambitions of the Commission and many MEPs to see the EU equipped with significant taxation powers.

²⁶ *European Voice*, “UK seeks support for tight post-2013 EU budget”, 17 Dec 2010, <http://www.europeanvoice.com/article/2010/12/uk-seeks-support-for-tight-post-2013-eu-budget/69782.aspx>

²⁷ *Europaortalen*, ‘Reinfeldt avvisar Camerons krav’, 17 December; <http://www.europaortalen.se/2010/12/reinfeldt-avvisar-camerons-krav>

²⁸ *Telegraph*, ‘David Cameron accused of ‘stitch-up’ deal with France to keep rebate’, 18 December 2010; <http://www.telegraph.co.uk/news/worldnews/europe/eu/8210544/David-Cameron-accused-of-stitch-up-deal-with-France-to-keep-rebate.html>

²⁹ *European Commission*, “Budget review: Lessons learnt for tomorrow’s budget”, 19 Oct 2010, <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/10/1351&format=HTML&aged=0&language=EN&guiLanguage=en>

3. An EU foreign policy?

The EU's new foreign service, headed by Catherine Ashton, the European External Action Service (EEAS), starts work on 3 January. The EEAS is very much a work in progress. Once fully operational, it is expected to have a staff of around 7,000. There are 136 EU delegations around the world, currently employing 2168 staff.³⁰ The EEAS also controls the EU's €7bn aid budget³¹. The EAS' ever-increasing budget will come under increasing scrutiny given the cuts facing national foreign ministries across Europe.

Overseas EU delegations are gradually being turned into EU embassies, providing consular services traditionally the job of member states, potentially supplanting their role.

Ashton also recently appointed the new head of the EU's intelligence-sharing bureau, the Joint Situation Centre – SitCen.³² SitCen brings together both external intelligence and internal security from across the EU, but few documents are publicly available on the nature of SitCen's work.

However, the EU's inability to come to common position on countries like Russia or even smaller countries like Zimbabwe continues to highlight the inconsistencies inherent in a common EU foreign policy.

4. Justice and home affairs

The EU's justice and home affairs budget will increase by 13.2% in 2011³³, reflecting the growing role of the European Commission, MEPs and the European Court of Justice in this area.

In 2011, the Commission will look into establishing a European Terrorist Finance Tracking Programme, following intense debates in 2010 about financial data sharing with US authorities. MEPs eventually backed an EU-US data sharing agreement on the condition that the EU establishes an equivalent to the US' terror financing tracking programme³⁴.

Negotiations, which the UK has opted into, on the controversial European Investigation Order³⁵ allowing other member states to request foreign police services to investigate suspects, including the sharing of DNA records, will continue. Agreement is expected some time in late 2011.

³⁰ http://ec.europa.eu/civil_service/docs/europa_sp2_bs_cat-sexe_x_dg_en.pdf,
http://ec.europa.eu/civil_service/docs/europa_sp2_bs_dist_staff_en.pdf

³¹ This includes: humanitarian aid, Development Cooperation, European Neighbourhood and Partnership and the Instrument for Pre-Accession Assistance. Ref: Europa, "EU budget 2010", http://ec.europa.eu/budget/library/publications/budget_in_fig/budg_2011_en.pdf

³² EUobserver, "Ashton picks Finn to be EU 'spymaster'", 17 Dec 2010, <http://euobserver.com/18/31541>

³³ *European Commission*, Draft General budget 2011, 26 November 2010, p4; <http://eur-lex.europa.eu/budget/data/P2011/EN/SEC00.pdf>

³⁴ *EP press release*, 'SWIFT II: Civil Liberties Committee approves draft agreement', 5 July 2010; <http://www.europarl.europa.eu/en/pressroom/content/20100705IPR77848/html/SWIFT-II-Civil-Liberties-Committee-approves-draft-agreement>

³⁵ *Telegraph*, 'Britons to be spied on by foreign police', 26 July 2010; <http://www.telegraph.co.uk/news/uknews/law-and-order/7909314/Britons-to-be-spied-on-by-foreign-police.html>

On the issue of asylum and immigration, the key developments over the next few years will be the Commission's long-standing attempts to establish a system of burden sharing for asylum applications, also described as a 'Common European Asylum System'. In 2011, the Commission is committed to reviewing member states' national asylum systems³⁶, with the ultimate aim of spreading the burden of accepting asylum applications that currently falls disproportionately on some EU countries.

The Commission will also review the implementation of the EU's Charter of Fundamental Rights, which was given full legal force under the Lisbon Treaty. A more active role for the Commission, backed by the ECJ, in 'enforcing' citizens' rights could well see greater confrontation with national governments. The Commission has pledged to "render effective the rights enshrined in the Charter for the benefit of all people living in the EU" by ensuring that national governments respect the Charter when implementing EU law³⁷.

5. The EU's new financial supervisors start work

In 2011, the EU's new financial supervisors – the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority – will begin operations. Initially, the authorities will be given binding powers over national supervisors in seven areas – in three of these areas the supervisors will have the power to address individual firms directly if national regulators do not comply with a decision. The supervisors will be allowed to interpret, apply and enforce provisions in over 20 separate EU laws. For the time being, day-to-day supervision will remain with national authorities, however. All decisions in the supervisors will be taken by either qualified or simple majority voting, meaning that the UK will in many votes have exactly the same voting strength as countries with almost no financial sector at all.³⁸

As Internal Market Commissioner Michel Barnier has said, the creation of the supervisors is only "a first step". There are currently several proposals in the pipeline which will be negotiated and possibly concluded next year, which could substantially boost the powers of the EU supervisors. In particular, ESMA is likely to grow in prominence. For example, under two proposals currently under negotiations, it could be given the final say over bans on short-selling, clearing of derivatives contracts and will also have an important role to play in the implementation of the AIFM Directive, which was passed earlier in the year. In addition, the EBA is likely to take an oversight role in the implementation of the EU's new rules on bankers' bonuses and will seek a facilitating role in stress tests for banks – which hopefully will lead to more coherent and rigorous tests than the ones undertaken earlier this year (see above). The authorities could also be given new responsibilities through the Commission's review of the MiFID Directive and amendments to the Capital Requirements Directive, for example.

³⁶ *European Commission*, 'Delivering an area of freedom, security and justice for Europe's citizens: Action plan implementing the Stockholm Programme', 20 April 2010, Annex 1, p56; http://ec.europa.eu/commission_2010-2014/malmstrom/archive/COM%202010%20171%20EN.pdf

³⁷ *European Commission*, 'Implementing the EU Charter of Fundamental Rights'; http://ec.europa.eu/dgs/justice/summary/docs/2010/implement_charter_FR_en.pdf

³⁸ For a more in-depth discussion on the supervisors, see Open Europe, "Shifting Powers: What the EU's financial supervisors will mean for the UK and the City of London", 6 September 2010, <http://www.openeurope.org.uk/research/EU supervisors.pdf>

Another outstanding issue that needs to be decided is who will chair the new supervisors, which is expected to be confirmed in April. The UK is hoping to secure the top position at the head of ESMA, which would be important given that this is the body which will become the most powerful initially³⁹. France is seeking to secure the EBA chair.

The Commission and MEPs are likely to push strongly for extending the mandate of the supervisors, either by adding new directives and regulations under the jurisdiction of the new bodies, or by making use of the so-called “review clauses” that can be used to augment the supervisors in future (though these clauses are unlikely to be invoked as early as next year). Moving forward, the UK Government would do well in intensifying its efforts to build alliances with countries around Europe, to ensure that the new supervisors are not hijacked by political or protectionist interests, to the detriment of the City of London.

6. Priorities for the Hungarian rotating presidency

From 1 January 2011, Hungary takes over the six-month rotating presidency of the EU, currently held by Belgium, handing over to Poland on 1 July. Hungary and Poland have announced that they are working closely to coordinate policies for what Hungarian Foreign Minister János Martonyi describes as a “Central Europe Presidency year”. Martonyi recently said that the Hungarian government sees its role as “diligent shepherd.”⁴⁰

On 10 November 2010 the Hungarian government adopted the draft programme of the Hungarian presidency, outlining four rather general priorities:⁴¹

- Economic recovery and social inclusion
- Stronger Europe – building on the foundations and saving the future
- A Union close to its citizens
- Enlarging responsibly and engaging globally

Hungarian Prime Minister Viktor Orbán has said, “We want a strong European Union, not a two-speed Europe, and to strengthen cohesion and cooperation in Central Europe”.⁴² Orbán outlined Hungary’s central priorities as energy security, Croatia's application for EU accession and integration of the Roma people, a subject that sparked controversy in 2010.⁴³

³⁹ *Handelsblatt*, ‘EU-Aufsichtsbehörden starten mit provisorischer Führung’, 21 December 2010; <http://www.wirtschaftspresse.biz/psepp/fn/pcc/sfn/showedetail/DocID/1127143/EditionID/4/SectionID/2/ParagraphID/1127129/pDay/21.12.2010%2000:00:00/showtyp/1/SH/47c122d91f3b7d33db366a011e41ed/index.html>

⁴⁰ *Euractiv*, “Hungary kick-starts ‘Central Europe presidency year’”, 21 December 2010, <http://www.euractiv.com/en/future-eu/hungary-kick-starts-central-europe-presidency-year-news-500818>

⁴¹ Hungarian Ministry of Foreign Affairs, “Priorities and programme of the Hungarian Presidency of the Council of the European Union in the first half of 2011”, http://www.mfa.gov.hu/kum/en/bal/european_union/eu_pres_2011/priorities.htm?kum2005/Templates/lapsablon.aspx?NRMODE=Published&NRORIGINALURL=/kum/en/bal/european_union/eu_pres_2011/priorities.htm&NRNODEGUID={2AC65415-D3EE-4775-827A-D4A3A37C96C6}&NRCACHEHINT=NoModifyGuest&printable=true

⁴² *Euractiv*, “Hungarian EU Presidency to kick off on energy”, 10 Nov 2010, <http://www.euractiv.com/en/priorities/hungarian-eu-presidency-kick-energy-news-499592>

⁴³ *EUBusiness*, 12 Oct 2010, “Hungary stands by deficit pledge: prime minister”, <http://www.eubusiness.com/news-eu/hungary-economy.6i4>

In an indication of Hungary's view on the EU budget, Hungarian Ambassador to France, László Nikićser, said earlier this year, "We need to develop new common policies [such as climate, energy or innovation], and then see how we can fund them, not vice-versa."

The EU's climate change ambitions are largely dependent on global climate talks, the key question being with the EU ups its emissions reduction target from 20% to 30% by 2020. The UK is a proponent of upping the target, with Energy Minister Charles Hendry saying, "We believe it can be done in a very realistic way without imposing significantly greater costs on consumers."⁴⁴ MEPs are also in favour of raising the target⁴⁵.

Given the current economic climate, there has been strong opposition from industry, particularly in Germany and Eastern Europe, to increasing the burden of climate change targets. Without a binding new global climate treaty, which looks unlikely given US and Chinese reluctance, the EU would be taking a reckless step if it unilaterally upped its target.

⁴⁴ *Bloomberg*, 'EU Should Target 30% Emissions Reduction by 2020, Hendry Says', 13 December 2010; <http://www.bloomberg.com/news/2010-12-13/eu-should-target-30-emissions-reduction-by-2020-hendry-says.html>

⁴⁵ *EP press release*, 'Climate: EU should move to 30% emissions reduction target, say MEPs', 25 November 2010; <http://www.europarl.europa.eu/en/pressroom/content/20101125IPR00549/html/Climate-EU-should-move-to-30-emissions-reduction-target-say-MEPs>

Annex 1: Calendar of key meetings and events 2011⁴⁶

January

- 1 Hungary takes over rotating Presidency
- 3 External Action Service becomes operational
- 23 Portugal – presidential election

February

- 4 European Council summit
- ? Irish general election

March

- 6 Estonia – parliamentary elections
- 20 Germany – Saxony-Anhalt state election
- 24-25 European Council summit. EU leaders will aim at agreement on treaty amendment for the eurozone's permanent bailout fund.
- 27 Germany – Baden-Württemberg state election
Germany – Rhineland-Palatinate state election

April

- 17 Finland – parliamentary election

June

- By June Commission to publish proposals on EU budget, including EU taxes.
- 24 European Council summit

July

- 1 Poland takes over rotating EU Presidency

September

- 4 Germany – Mecklenburg-Vorpommern state election
- 18 Germany – Berlin state election

November

- 12 Denmark – parliamentary election

⁴⁶ <http://europa.eu/eucalendar/>