THE POST-2013 EU MULTIANNUAL FINANCIAL FRAMEWORK:

TIME TO BE BOLDER

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1 THE POST-2013 MULTIANNUAL FINANCIAL FRAMEWORK – THE NEED TO GET IT RIGHT

Agreeing the post-2013 Multiannual Financial Framework (MFF) is one of the most critical political challenges lying ahead for the European Union (EU). Altercations over the size of the budget already are running ahead of debate over substance, the direction of spending and indeed the precise source of funds. One group of Member States, including France, Germany and the UK has been quick to propose freezing the budget at the present level, invoking the principle of shared austerity, provoking a strong defence of EU expenditure from Poland and others. A great number of such exchanges and sub-plots lie ahead before this piece of political theatre is concluded.

This should not, however, obscure debate on how the funds should be spent in an efficient way in support of the key priorities for Europe. Understandably, the most pressing worry for heads of states and governments is how Europe will get out of the economic crisis. However, a business-as-usual approach will not suffice here. Making the transition to a low-carbon, resource efficient economy cannot be postponed for another decade. There is no choice but to build this goal into forthcoming plans for a sustainable economic recovery and consequent action to promote competitive industries, innovative technologies and stable jobs. A key priority for the next MFF therefore is to achieve a shift in the European economy so that it is greener measured both by carbon efficiency and by overall environmental performance and is also creating new skills, jobs and investment towards recovery. The environment, including the climate dimension, is integral to this agenda and must be recognised as such. Conversely, **the next MFF is more important for the environment and the sustainability of the European economy than any of its predecessors.**

The discussion about the next MFF comes at a time when major turning points in Union policy are being approached. Long-term roadmaps for critical areas such as climate change and energy and resource efficiency are currently being developed under the Europe 2020 Strategy process. Strategic proposals on the Common Agricultural Policy (CAP), Cohesion Policy, funding for the environment and other topics will be published this summer. All have a budget dimension, in short**, the priorities for the next decade extend well beyond the Europe 2020 agenda and the post-2013 MFF should not be confined to this economic strategy**.

In the run up to the legislative proposals on the post 2013 MFF due in June 2011, this policy brief offers a short analysis of some critical aspects of the debate and outlines a set of ‘stepping stones’ for strengthening the environmental dimension of the proposals.

Why is the post-2013 MFF important for the sustainability of the EU economy?

- First, there is a historic opportunity to step back and *align the budget more closely with the EU's longer term objectives*. Sustainability and the construction of both a greener and a lower carbon economy are recognised as critical directions of travel, not least in Europe 2020, and there is now the potential to reflect this in the EU budget. Conversely, failure to do so will signal a clear lack of commitment to the new agenda. The stakes have got higher;

- Second, spending under the MFF will have an influence on the *infrastructure of the future, not just in energy supply, transmission and conservation, but in transport, water, urban design and rural structures*. These are the building blocks of a green economy and very large investments are required both within and between Member States. A substantive change in the public support for investment needs to be made during the critical period up to 2020 when the foundations of a green economy for 2050 need to be laid. EU funds can play a pivotal role not only in the direct support of investment but also in exerting leverage over other streams of public and private spending. A *clear strategy for innovative financial instruments is imperative*, including a fresh look at the EIB's mandate and priorities in this direction;

- With a clear vision, changes can be introduced in nearly all EU funds to *improve the focus, coherence and effectiveness of expenditure*. Mechanisms to minimise investments in high carbon infrastructure could be introduced for example. Since it is highly likely that there will be more EU level Strategic Guidelines of some kind steering expenditure under all the funds in a coordinated way, it is especially critical that these reflect environmental priorities. There would be an opportunity to support concepts such as carbon proofing for example;

- In addition to a role in assisting the *take-off of a greener economy*, the EU budget has the potential to address two areas of contemporary environmental crisis; the structural over-exploitation of European fish stocks and the continued decline of biodiversity and wider natural capital, particularly on farmland. EU interventions, including through the CAP, Common Fisheries Policy (CFP), LIFE+ and several other funds will be critical determinants of the outcome; and

- The debate on the *revenue side of the budget, while still tentative, also has potentially large implications for the environment*. Were a new form of 'own resources' to be accepted, many of the more credible options for raising funds would be in the realm of green taxation, potentially complementing other forms of intervention but opening a particularly contentious political debate.

2 STRATEGIC ORIENTATION AND PRIORITIES

The EU Budget Review Communication which was published last autumn is an important point of departure for discussion. ***It is helpful in highlighting the need to spend the European budget more intelligently, as opposed to focussing largely on how much more or less should be spent.*** To this end, it outlines principles for concentrating funding on key priorities with concrete European added value, aiming to fill gaps and help important projects reach a critical mass. While the need to focus on results gets some attention, the Communication fails, however, to give any decisive orientation for change in key spending areas, leaving many questions open as regards concrete priorities, and consequently the added value of EU spending. Generating the political momentum needed among EU Member States and key stakeholders becomes difficult when the signposts are so reticent.

While all the primary policy objectives on the EU agenda are potentially relevant to the MFF the Commission seems to have chosen to align it almost exclusively on the priorities set out in the Europe 2020 Strategy process. This link offers opportunities for scaling up action on climate change mitigation and resource efficiency but otherwise seems overly restrictive. Wider environmental considerations and options for a genuine 'greening' of future spending are completely integral to the budget debate even if they involve topics that are not in the forefront of Europe 2020, such as Cohesion and agriculture.

For example, the Communication does not explicitly consider biodiversity and climate change adaption funding, nor does it really address policies to tackle Europe's resource constraints in a world that is interlinked and inter-dependent to an unprecedented degree. ***Yet adjustments at the margins will not deliver a low-carbon, resource efficient economy.*** Such omissions could create the basis for serious future policy failures. Our natural capital underpins the well-being of our economies and societies, as the UNEP Economics of Ecosystems and Biodiversity (TEEB) initiative has shown convincingly. It is apparent from work within IEEP and elsewhere that considerable sums are required to provide the level of environmental public goods that Europe already has committed itself to pursuing through adopted legislation and formal targets, but that the economic and social benefits received in turn are very considerable. The mandate is clearly there.

Maintaining and improving Europe's global competitiveness and the fight against climate change came out as the most significant future challenges which needed to be reflected in the budget from the public consultation (SEC(2008)2739). Low carbon and resource efficient technologies and jobs continue to receive widespread public support and this is a further reason for having the political coverage to drive a shift in priorities. What is required now is to become much more explicit and substantive about the objectives and instruments at hand.

Value added by European spending will continue to be an important criterion for directing funds and making judgements about the scale of resources required. This needs to be understood at more than one level. There are well rehearsed considerations such as the need for the EU to address issues that can be tackled only at a European level, exemplified by Cohesion Policy and cross-frontier questions. There is then another set of issues which are more efficient or feasible to address at the EU level for technical or economic reasons, such as the development of certain new technologies (European wide smart grids is an often quoted example). However, there is also a much broader political dimension to EU value added. ***The budget needs to recognise Europe's changing identity, its direction of travel and the issues that inspire the future. The budget needs to move on from previous preoccupations to new ones.*** In this respect the environmental dimension and its climate component are underweight in the current budget and the balance must change. The post-2013 MFF should contribute to the coherence of the Union in a way that resonates with the public more strongly in the CAP and Cohesion policies which account for so much expenditure.

The focus on EU value added while important is not enough. There is a need to strengthen the quality of spending and its effectiveness. Achieving transparency is a key challenge. These concerns need to be prominent in the next proposals from the Commission. ***A results driven EU budget would itself be a contribution to increasing value added post-2013***.

3 THE THEMATIC CHALLENGES

3.1 Climate Change

Climate change as an issue cuts across several different axes of the current budget debate. Both the expenditure and the revenue side of the EU budget are involved. On the expenditure side, four issues are of particular relevance. These include the potential role of a new dedicated climate fund, strategies to re-focus existing environmental funds and concrete mechanisms to streamline climate change concerns into other sectoral funds. The use of more novel mechanisms such as bonds and new lending facilities to extend leverage beyond the present budget is a fourth challenge.

There is considerable backing from EU Member States and a wide range of stakeholders for ***scaling up the role and relevance of climate related investment in the EU budget.*** The consultation process on EU budget reform back in 2008 provided ample evidence. The draft Communication leaked in 2009 gave reason for hope: it contained a proposal for a *European Framework Programme for Climate and Energy* targeting direct spending on climate change and energy priorities and called explicitly for the 'climate proofing' of both Cohesion Policy and CAP related expenditure.

One year later not much of this ambition appeared to survive. The Budget Review Communication no longer mentions the idea of a *Framework Programme* and the call for climate proofing the EU budget. Climate change and energy are presented as part of critical but rather different discussion on sustainable growth. The option of mobilising large-scale, dedicated funds for the delivery of greener technologies is raised. However, it is put down again in favour of an approach purely based on 'mainstreaming', which is rather sketchily described in two paragraphs. The discussion of the primacy of policy goals like climate change and energy is helpful and seems to point to a 're-prioritisation inside policies like research, cohesion, agriculture and rural development – with a clear political earmarking balanced by the need to avoid new rigidities'. Does this mean more ring fencing of funds for climate goals?

Despite the caution in the Communication and the likely reluctance in many Member States to accept a growth in the number of EU funds, a separate climate change instrument offers a number of advantages. It is simply premature to reject this option at this stage of the political discussion. There are funding gaps and opportunities to address and even a moderately resourced fund could break new ground. For both governments and other investors and stakeholders it could help to generate enhanced political priority for climate goals where such is absent and set examples of good practice models in terms of effectiveness per euro spent. If this approach is not allowed to fly, mainstreaming as the preferred policy approach needs to be considerably strengthened and made more explicit, including concrete provisions for ring-fencing of dedicated funding directly targeting climate change mitigation and adaptation measures.

In addition to scaling up the support for climate change measures in the next MFF existing spending in other areas needs to be scrutinised and amended, to ensure that it is not counter-productive to climate mitigation efforts. The debate about how we might go about climate proofing the EU budget is already well underway. An expanding menu of options is developing. Importantly, the overall impact of the post-2013 MFF on the Union's greenhouse gas balance should be assessed and the most significant climate change drivers formally identified. Carbon intensive activities receiving significant funding need to be spotlighted and assessed and steps towards reform and the phasing out of support should be drawn up. Secondly, climate change mitigation and adaptation measures should be horizontally integrated across all sectoral spending through the introduction of procedures such as setting specific minimum requirements, project selection criteria or encouragement of green public procurement. Appropriate institutional capacities are a significant factor for success at all levels of governance. The post-2013 MFF needs to actively support capacity building, to the extent that existing support measures under environmental funding programmes such as Life+ are extended for this purpose.

Overall, climate proofing the EU budget needs to be seen in a longer-term perspective up to 2050; 2020 is a milestone by when concrete and workable strategies and tools need to be in place. Otherwise, the corridor of opportunities to address climate change meaningfully risks encountering a premature dead-end.

3.2 Biodiversity

Since the launch of the 2005 Millennium Ecosystem Assessment we have known about the pivotal role of ecosystems and their services for human well-being. The Commission itself has put considerable efforts into establishing the global UN TEEB initiative and has declared that the persistent decline of biodiversity and degradation of ecosystems cannot be detached from long term economic sustainability. So it is all the more surprising that the whole dimension of maintaining Europe's natural capital is invisible in the autumn Budget Review Communication. The conservation and sustainable use of biodiversity is only addressed marginally, in the context of the CAP. Evidence is piling up that directing funding to well chosen biodiversity projects positively supports sustainable development and growth, and in this way investment in nature can more than pay for itself. On the other hand, the loss of ecosystem services (ie natural resources and processes underpinned by biodiversity) at its current pace is likely to amount to hundreds of billion euro over the coming decades.

Indeed the EU has completely missed the strategic objective of halting the loss of biodiversity by 2010 partly because there has been inadequate financial support for conservation measures which have strong regulatory backing through the EU Birds and Habitats Directives. The EU has now committed itself to a new and ambitious target on halting the loss of biodiversity and ecosystem services and to restore them as far as possible by 2020. This should be taken seriously. ***A clear reference in the proposal for a post-2013 MFF on the challenge of meeting the new biodiversity target and the role of different funds in contributing to the EU's share of costs would inject new impetus into this debate and remove one obstacle to progress.*** It is striking that the principal EU financing instrument to support environmental and nature protection, Life+, is not addressed even once in the Communication.

The Resource Efficiency flagship initiative is one area within the Europe 2020 Strategy where this agenda can be addressed, alongside other issues. It needs to recognise the role for promoting natural ecosystems that fulfil functional roles, such as providing clean water, fixing carbon and contributing to flood control. The EU budget is an essential policy tool in this respect, promoting joined up policies and new ways of thinking. ***Strategies for future infrastructure investment need to incorporate softer and more natural elements and more resilient ecosystems, for example in relation to water and flood management.*** These are often cost effective as well as sustainable and compatible with conservation goals. As one of the most important public goods associated with land and marine management, there should be a strong European interest in securing adequate funding to protect biodiversity more effectively in the future, not only in the core environmental fund, LIFE+, but also in the CFP and CAP. For all these reasons biodiversity should not be neglected in the EU budget.

3.3 Common Agricultural Policy

While the future size of CAP expenditure often is the issue attracting the greatest attention in the budget debate it is the rationale for and direction of this expenditure that is the greater litmus test of the sustainability of the MFF. The Budget Review Communication was accompanied by the Commission Communication on proposals for the CAP in 2020 (COM(2010)672) within a matter of weeks and they are largely consonant with one another. They do signal some new directions, including a significant proposal to 'green' Pillar One, the single most important element of the CAP. However, ***an opportunity has been missed to clearly refocus the CAP on the provision of public goods with the potential to contribute significantly to the delivery of a number of key environmental objectives in Europe.***

Under the heading of 'Sustainable Growth', the paper does highlight the importance of agricultural policy for achieving a wide range of EU objectives, including 'cohesion, climate change, environmental protection and biodiversity, health and competitiveness, as well as food security'. However, this is not developed further and the real significance of adopting a new rationale for the expenditure of public money is not spelled out.

Within the context of the broader CAP debate there has been an emerging consensus that the current rationale for substantive expenditure on agriculture, forestry and land management is no longer appropriate. By contrast, there is a real need to increase the provision of environmental and social public goods in rural areas. For example, it will be difficult to meet biodiversity targets without a significant change in farm and forestry management on a European scale driven by incentives for land managers as well as regulation, advice and exhortation. So it is all the more surprising that the term 'public goods' is not mentioned in the Budget Review Communication at all. Instead it is focussed on the way in which the CAP could be used to meet the Europe 2020 Strategy objectives, stressing the contributions that a 'sustainable, productive and competitive agricultural sector' can make to 'enhancing the growth and employment potential of rural areas while ensuring fair competition'. Environmental priorities are largely seen as a means of underpinning the achievement of these social and economic priorities. Whilst the economic health of the agriculture sector is clearly important this formulation fails to capture the significance of what could be achieved by a focus on public goods and the real need to invest in the rural environment and its management.

At an instrumental level, the Communication does make it clear that the current decoupled direct payments under Pillar One, based largely on historic production levels in the EU-15, are no longer tenable. Indeed it goes further to suggest that they promote 'a culture of dependency which may hold back the use of incentives to ensure that results are delivered'. Despite this, alternative means of pursuing the CAP Communication goals of viable food production, sustainable management of natural resources, and balanced territorial development are explored only in very general terms. This lacuna understates the importance of the CAP from an environmental perspective and so contributes, inadvertently, to a lop-sided debate on the budget as a whole.

3.4 Cohesion Policy

After the CAP, Cohesion Policy constitutes the second largest share of the EU budget, which is also going through its own reflection process. As the stakes are rather high, especially for new Member States which are among the main recipients of the funds, there is likely to be quite strong resistance to any dramatic change (as demonstrated by Poland which presented its less than ambitious position on the future Cohesion Policy last August). At the same time, there is growing evidence that ***European regions are faced with new challenges, amongst them globalisation, demographic change and new social concerns, climate change and the need for new energy investment. Political choices for new development pathways need to be made soon***.

It is no surprise that the EU Budget Review Communication remains generally vague on this policy. What it does though, is to pitch in a number of interesting ideas, for example, introducing qualitative competition among programmes for Cohesion funding; setting up a performance reserve to reward front runners; and modulating co-financing rates according to performance. These can all give valuable signals to Member States. Yet important questions remain: how will priorities be selected, how will performance be defined and measured and, most importantly, how should all of these actions be geared to environmental, low-carbon and resource efficiency objectives and targets? The forthcoming legislative package on the post-2013 MFF has to come clearer on all these issues, especially in view of the proposed Common Strategic Framework and the so called special development and investment partnership contract. If adopted, these may imply a more top-down approach in the future Cohesion Policy.

Some of these ideas were taken forward in the 5th Cohesion Report adopted in November 2010 (COM(2010)642), a document that needs to be read in conjunction with the EU Budget Review Communication. Importantly, the environmental perspective is significantly strengthened, both in relation to the sustainable growth objective of the Europe 2020 Strategy but also as an intrinsic element of defining and achieving 'territorial cohesion' (the new objective introduced by the Lisbon Treaty). The opportunities for environmental investments to create new, green sources of growth and employment are also clearly indicated. Furthermore, it has been recognised that the vision of 'harmonious development' underpinning Cohesion Policy includes not only economic development and support to social groups but also 'environmental sustainability and respect for the territorial and cultural features of different parts of the EU'. In this sense, ***the vision of development being offered from the Cohesion corner is broader compared to the Europe 2020 Strategy and has a clear place-based dimension.*** While positioning the future Cohesion Policy in the framework of the Europe 2020 Strategy could achieve greater focus and concentration of resources on fewer but strategic objectives of European importance, there is a danger that it would in fact be likely to establish a rather narrow and unimaginative vision of the European development model and the future of regions.

Following this logic, a dynamic reform of EU Cohesion Policy is required inspired by the urgency of emerging challenges, which needs to be reflected in the final proposal for the post-2013 MFF. ***A truly progressive reform agenda would question the very fabric of Cohesion Policy and help to redefine the development paradigm beyond GDP per capita while offering a more holistic perspective in terms of sustainable development pathways, particularly in relation to climate change, resource efficiency and green infrastructure.*** If impetus can be gained from this direction it will help to address the environmental deficit in the MFF beyond 2013.

4 REFORMING REVENUES – OPTIONS FOR GREENING THE BUDGET

The issue of new 'own resources' for the EU budget has resurfaced with new strength in the context of national austerity and budget consolidation. This could be seen as a window of opportunity to appraise alternatives to at least some of what is currently three quarters of the EU budget revenues, ie direct contributions from Member States, as it offers a way of reducing the pressure on their balance sheets. ***If direct contributions are balanced out with other sources of financing, there will be a stronger incentive to shift the focus of budgetary negotiations from national shares and correction mechanisms to the more fundamental role of the EU budget as a complement to other policies and a directional driver.*** A system of new own resources could further improve the transparency of the financing system and create stronger accountability and independence on the expenditure side. The Commission has a clear interest in this and the issue is prominent in the Budget Review Communication. It puts forward quite a bold non-exclusive list of 'potential candidates' for generating revenue which include an EU VAT, taxation on the financial services sector, on aviation, on energy, on corporate income and auctioning of EU-ETS allowances. In addition, the Commission has reiterated several times since then its determination to table a proposal for a Draft Decision on new own resources in June 2011.

While the moment might appear ripe for the Commission, taxation at EU level is a politically sensitive issue for many Member States on the grounds of subsidiarity and even democratic legitimacy, which historically has impeded progress in this area. Furthermore, change would require unanimity in the Council and ratification by all national parliaments. While some support for an EU tax seems to be emerging in Spain, Poland, Austria and Belgium, the UK and Germany have voiced strong opposition, which indicates that it will be difficult to get all Member States on board, however strong the arguments at a European level might be. The European Parliament on the other hand appears to back the Commission on the need for new own resources but considers the overall prospects of brokering a deal as unrealistic. It is possible that the European Parliament will gain greater leverage in the budget debate and they could utilise the nostrum of 'no taxation without representation' in support of their cause. ***Given these and other uncertainties about inter-institutional relations and the wider politics in this area it would be unwise to dismiss the whole question of creating new sources of revenue as politically unfeasible.***

Consequently, the proposed candidates for revenue raising deserve some substantive consideration. Article 311 of the Treaty on the Functioning of the European Union (former 269 of the TEC) prescribes that 'without prejudice of other revenue, the budget shall be financed wholly from own resources' and thereby provides a legal basis for establishing new categories of own resources. The public finance literature suggests that possible options should be assessed against criteria such as sufficiency, stability, visibility, equity, operational costs, efficient allocation of contributions and fair distribution. These are tough conditions to meet but it is also clear that there is potential to advance policy in the environmental sphere at the same time as diversifying EU revenues if appropriate options were selected.

Environmental taxes are in principle complementary to other policies pursuing climate objectives in Europe and could raise considerable sums. Related revenue estimates need to be updated and some difficult questions addressed, such as the distribution of burdens on different Member States. Still, the energy tax alone is considered to be relatively stable and capable of generating a significant part of the EU budget while bearing little administrative cost. The EU-ETS auction revenue is another potential candidate widely discussed in the last few years. ***The merit of environmental taxes or ETS auction revenues is that they can be geared to EU ambitions with respect to climate and energy policies while fostering wider behavioural changes in consumption patterns and production processes.*** This justifies further debate, despite the substantive objections and understandably sensitive issues involved.

5 CONCLUSIONS

The economic crisis and subsequent climate of austerity in much of Europe may seem to have cut the room for manoeuvre for a substantive recasting of the European budget. At the same time, the heated debate about the size of the EU budget has overshadowed deeper dialogue on the composition and quality of EU spending. However, these issues must return to the foreground over the next few months. With their strong focus on net balance, governments risk a budget that is too compromised to offer a sense of clear direction or to support critical policy development where strategic expenditure is essential. The political implications of such a failure could be large, leading to further problems in both securing EU added value and communicating it to Europe's citizens in times when public budgets are under pressure everywhere. Given the sweeping changes in the geo-political context as well as the difficult challenges that are waiting at home, ***it would be extremely costly to compromise on a budget that is firmly stuck in the past.***

The drive for greater effectiveness and focus on results in the MFF would support the pursuit of a greener trajectory. It could include a stronger commitment to the removal of support for unsustainable activities and the use of new approaches, such as climate proofing the budget. Currently it is often more than difficult to determine what large sections of the budget are spent on in concrete terms. Tools to remedy the situation would include well considered EU Guidelines, the selected use of ear-marking of certain funds, intelligent eligibility rules, stronger monitoring and evaluation procedures and a general insistence on transparency. The established inspection and auditing culture needs to be supplemented by more positive investment in capacity building by Member States, with EU aid through technical assistance.

This will require some adjustment but attempts to dismiss an added-value, results-driven approach as too bureaucratic should be resisted. Tools such as climate-proofing can provide useful information on economic efficiency as well as environmental effectiveness and lead to a helpful prioritisation of investment.

The EU budget is small in relation to Europe's GDP. Nonetheless, it has the potential to signal and help to steer changes in direction, support several strategic policies, leverage in further funding from European and national sources and build new capacities. It has under performed in relation to the environment and has yet to address the climate agenda to the necessary degree. Greater ambition is now required.

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