

EUROPEAN UNION



**Committee of the Regions**

# **The Future of Cohesion Policy**

## **Report I**

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# List of abbreviations

Abbreviation	Full term
AA	Audit Authority
AECT	Agrupamento Europeu de Cooperação Territorial
CA	Certifying Authority
CAP	Common Agricultural Policy
CBC	Cross-border cooperation
CEF	Connecting Europe Facility
CF	Cohesion Fund
CETC	Central European Transport Corridor
CEO	Central Executive Officer
CIVEX	Commission of Citizenship, Governance, Institutional and External Affairs of the Committee of the Regions
CLLD	Community-led Local Development
COESIF	Coordination Committee for the ESIF
COPIT	Cross-Border Standing Conference of Inter-municipal Organisations
CoR	Committee of the Regions
COTER	Commission of Territorial Cohesion Policy of the Committee of the Regions
CP	Cohesion Policy
CPR	Common Provisions Regulation
CSR	Corporate Social Responsibility
DG	Directorate General
EAFRD	European Agricultural Fund for Rural Development
EAGGF	European Agriculture and Guidance and Guarantee Fund
EC	European Commission
ECF	European Cohesion Fund
ECOS	Commission of Economic and Social Policy of the Committee of the Regions
EDUC	Commission of Education, Youth, Culture and Research of the Committee of the Regions
EETAA	Hellenic Agency for Local Development and Local Government
EEIG	European Economic Interest Grouping
EfD	Expenditure for Development
ESIF	European Structural and Investment Funds
EGTC	European Grouping of Territorial Cooperation
EIB	European Investment Bank
EIF	European Investment Fund
ENVE	Commission of Environment, Climate Change and Energy of the Committee of the Regions
EP	European Parliament

ERDF	European Regional Development Fund
ESF	European Social Fund
ESIF	EU Structural and Investment Funds
ETC	European Territorial Cooperation
FDI	Foreign Direct Investment
GBER	General Block Exemption Rules
GDP	Gross Domestic Product
GFCF	Gross Fixed Capital Formation
GHG	Green House Gas
GNI	Gross National Income
ICT	Information and Communication Technologies
IP	Investment Priority
IPA	Instrument for Pre-accession
ITI	Integrated Territorial Investment
JAP	Joint Action Plan
JTS	Joint Technical Secretariat
LRA	Local and Regional Authorities
MA	Managing Authority
MC	Monitoring Committee
MEP	Member of European Parliament
MLG	Multi-level Governance
MS	Member State
MTO	Medium-Term budgetary Objectives
NAT	Commission of Natural Resources of the Committee of the Regions
NGO	Non Governmental Organisation
NSRF	National Strategic Reference Framework
OP	Operational Programme
PA	Partnership Agreement
PPP	Public Private Partnerships
RAG	Regional Aid Guidelines
RCE	Regional Competitiveness and Employment
RDTI	Research, Technology Development and Innovation
REGI	Committee of Regional Development of the European Parliament
SAPARD	Special Accession Programme for Agriculture and Rural Development
SEDEC	Commission for Social Policy, Education, Employment, Research and Culture
SF	Structural Funds
SCP	Stability and Convergence Programme
SGP	Stability and Growth Programme
SGEI	Services of General Economic Interest
SME	Small and Medium Enterprises



SPF	Small Project Fund
STI	Science, Technology, Innovation
UDN	Urban Development Network
TCP	Transnational Cooperation Programme
TO	Thematic Objective
VET	Vocational Education and Training
YEI	Youth Employment Initiative



# Executive Summary

The report Future of cohesion policy examines the main issues of debate around the cohesion policy in order to set up the political framework of discussion. Methodologically, this first report is based on an analysis of past debates, predominantly in regional EU fora. Desk-based research was supplemented by thematic discussions with other EU institutions, experts and key stakeholders in the scope of a seminar. Furthermore this study series on the Future of cohesion policy should provide a new impetus to the work of the Committee of the Regions and its members in the policy debates on the efficiency and effectiveness of Cohesion Policy from the perspective of local and regional authorities as well as the main topic of the research: The Cohesion Policy beyond 2020. Hence and following the order form the main work is divided into two reports:

- Report 1– should outline trends and major aspects of effectiveness, efficiency and governance related to Cohesion Policy from the perspective of local and regional authorities.
- Report 2– should present models and ideas for the future of Cohesion Policy (elaborated until November 2015).

This current Report 1 itself is again divided into two parts. Part one covers the gaps, trends and challenges with its impact at regional level. Part two is about the effectiveness, efficiency and governance of Cohesion Policy at regional and local level.

## **Part 1: Gaps, trends and challenges with impact at regional level**

This component analyses challenges at local and regional level linked to the impact of the crisis and a long period of low economic and employment performance, the regional and local impact of major trends impacting economic, social and territorial cohesion and challenges of the growing economic, social and territorial divide as well as the challenges for LRA authorities arising from the trend towards centralisation of EU economic and monetary policies.

The analysis and review of sectoral developments and the related territorial implications at the beginning serves to set the scene for the subsequent part of the report which is focussed on implementation. The intent is to briefly review trends and challenges from a sectorial perspective, the major territorial implications and thus the major challenges for LRAs and the implications for Cohesion Policy.

The structure of the ESIF is still markedly oriented on economic sectors, thus the major expectable trends in the three traditional sectors 'Agriculture and Forestry', 'Manufacturing and Industries' and the 'Service sector' are outlined with its visible as well as expectable major territorial implications:

**Table 1. Major trends in social, economic and territorial cohesion per sector**

Sector	Major trends	Social Cohesion	Economic Cohesion	Territorial Cohesion
Agriculture	Intensification and polarisation, Liberalisation and global competition Cost pressure, Environmental externalities, Emergence of agro-environmental and ecosystem services approaches Depopulation and marginalisation, Changes of land uses (abandonment, use for leisure)	Need for diversification and supply of employment and production processes, Need for safeguarding education and training opportunities, Preservation of a just taxation base, Respect of minimum social standards, Need to enable local livelihoods, Need to address increasing social segregation and spatial polarisation, Need to accommodate the “globalisation losers” and the marginalised groups, Importance of social innovation and effective governance modi,	Need to adapt to the global competition, Need to ensure sources for capital investments, Need to enable integration and exploitation of technological advances, Need to decouple growth from (imported) resources, Need to provide or attract highly skilled/diversified personnel, Need to provide cost-efficient services of general interest and infrastructures and ICT, Need to provide for a framework that favours innovation (standardisation, IPR protection, financing, support etc.) Need to provide for compensation schemes for the provision of public goods and safeguarding of common-pool resources Need for Innovation Need for Standardisation	Need to introduce area based policy approach (instead of sectoral), Need to enhance centre-periphery cooperation, Need to overcome locational disadvantages and/or valorise local advantages, Need to adapt infrastructure to the trends and ensure cost-efficient connectivity and services, Need to stop marginalisation and out-migration, Need to integrate migrants
Industry	Integration in global value chains, Standardisation, Global competition, Interweavement with services, Division of labour and regional demand for specific skills, Increasing disparities for peripheral areas, Polarisation effects and vicious circles, Staggering resource consumption, Rehabilitation costs			
Services	Tertiarisation, Increased demand due to increased living standards and production processes, Innovation drive crating new services, Delocalisation of industries, Increase of precarious jobs, Growing demand for social services, Growing demand for labour market interventions			

Perspectives for LRA Action			
Regulatory acts	Definition of required minimal skills	Definition of operating conditions (e.g. permits) Obligation for minimal standards and CSR provisions Protection of employee rights	Definition of spatial opportunities and restrictions, Definition of minimum standards for each territory
Incentives	Provision of infrastructures Fostering of Social Innovation and governance Incentives to invest in skills Incentives for the development of services,	Provision of fiscal incentives, Provision of infrastructures	Provision of fiscal incentives, Provision of infrastructures, Provision of flexible infrastructure to respond to local needs,
Information and Motivation	Fostering of Social Innovation and governance Foster CSR,  Strategies to attract stakeholders in becoming active	Marketing/Branding	Marketing/Branding

*Source: own considerations.*

The review of the sectorial developments is combined with a review of trends and territorial implications in selected key sectorial policies which are closely interlinked with Cohesion Policy. These are:

- Environment, climate change adaptation, low-carbon economy and resource efficiency.
- Labour market and social policies, health care.
- Education and qualification.
- Research and Innovation.
- Network development and infrastructure.
- SME policy.

The policies were pooled along similar development logics such as key items for EU12/13, the establishment in MS considering the responsibility of line ministries, the focus on technology development, comparable planning logics and the implementation across sectors as well as access to financing.

It is important for the whole report and the following papers for the future of Cohesion policy to limit the number of policies being discussed since the intent is providing a comprehensive albeit readable document. The approach above is a rough clustering where policy areas which follow similar development logics have been pooled.

The role of EU sectorial policies and the opportunities and implications for the tasks for LRAs are summarised as follows:

**Table 2. The role of EU sectorial policies and opportunities and implications for the tasks for LRAs**

<b>Sectorial Policy</b>	<b>Major Trends</b>	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Environment, climate change adaptation, low-carbon economy and resource efficiency	<p>The Water Framework Directive is the cornerstone of water resources protection demanding an integrated long term ecosystem approach;</p> <p>Waste is turned into a resource;</p> <p>Waste minimisation is preferred over waste management and disposal;</p> <p>Climate change affects the availability of water resources ;</p> <p>Biodiversity as a guarantee for the sustaining of ecosystem services and human welfare;</p> <p>Resource efficiency is a global competition factor affecting all aspects of production and consumption</p>	<p>Restrictions/pricing on resources use and disposal</p> <p>Alternative job opportunities,</p> <p>Spatial planning and zoning,</p> <p>Risk management and voluntary organisations,</p> <p>Creating local green markets</p>	<p>Restrictions/pricing on resources use and disposal</p> <p>Demand for Eco-innovation, technological solutions, monitoring etc.</p> <p>Demand for innovative and efficient management practices</p> <p>Investments for climate change mitigation and adaptation</p> <p>Spatial planning and zoning, risk management and location selection,</p> <p>Response to degradation of ecosystems and the need to adapt to the loss of environmental public goods</p> <p>Promotion of partnerships for resource efficiency and definition of standards</p>	<p>Integrated management approaches beyond administrative borders</p> <p>Construction and operation of public utilities networks, physical infrastructure and other related works</p> <p>Spatial planning and zoning,</p> <p>Risk management,</p> <p>Valorisation of biodiversity and natural heritage</p>
Labour market and social policies, health care	<p>Increasing unemployment;</p> <p>Increasing atypical forms of employments;</p> <p>Polarisation and accentuation of poverty risks;</p> <p>Demographic transition and ageing society ;</p> <p>Need for flexible social services, e.g. childcare ;</p> <p>Migration.</p>	<p>Provision of locally adapted social services</p> <p>Provision of support services for escaping poverty traps</p>	<p>Enabling work life balance</p> <p>Enabling economic activity and employment of disadvantaged groups</p> <p>Creation of incentives for entrepreneurship, employment etc.</p>	<p>Mobilisation of area based tools such as CLLD, IT etc.</p>



Education and qualification	Young unemployment as a result of poor skills; Mismatch of labour market needs and education/training offerings; Education and training as prerequisites for social integration; Poor qualifications recognition of migrants.	Local adaptation of offerings	Local employment agreements (e.g. TEP)	Mobilisation of area based tools such as CLLD, IT etc.
Research and Innovation	Increasing dispersion of business activities; Competition for high value activities in Global Value Chains; Accelerated knowledge flows between interconnected knowledge hubs and polarisation; lagging behind regions cannot catch-up;	Provision of skilled labour forces Attractiveness as residence choice for highly skilled R&D personnel	Provision of locations, Spatial planning and zoning, location selection support, Development of auxiliary services (e.g. non basic sector)	Management and implementation of tools like the RIS3 Creation of “innovative” regions in the context of the JRC key elements (niche products, securing of resources and conditions, overcoming path-dependency)
Network development and infrastructure	Investments in the TEN (differentiation among core and comprehensive network) Mobilisation and coordination of investment sources, Increase in traffic flows, “containerisation” and multimodal hubs, New logistic concepts and need to keep pace with capacities Increasing environmental considerations	Provision of “accessibility justice”	Provision of infrastructure as a location selection factor Integrated management “real time” approaches Integration of energy supply and demand in the infrastructure provision and location endowment	Integrated management approaches Construction and operation of public utilities networks, physical infrastructure and other related works Spatial planning and zoning, Risk management,

SME policy	<p>Recognition of the role of SMEs</p> <p>Extensive specific administrative burden for SMEs.</p> <p>Difficulties in access to finance</p> <p>Limited access to public procurement</p> <p>Modernisation of bankruptcy procedures and abolition of social and administrative stigmata</p> <p>Entrepreneurial education</p> <p>Integration of SMEs in Global Value Chains</p>	Facilitation of entrepreneurship	<p>Provision of locations, Spatial planning and zoning, location selection support,</p> <p>Development of auxiliary services (e.g. non basic sector) and intermediaries</p> <p>Provision of loan facilities</p>	<p>Territorial partnerships</p> <p>Provision of attractive environments</p>
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*Source: own considerations.*

## **Policies for specific regions**

Despite the evident dominance of sectorial approaches in most MS the aspect of the policy focus on specific regions must not be forgotten. In part the EU provisions for Cohesion Policy do foresee or shape incentives in that sense. In part some MS have such approaches which have been / are being reinforced by EU Cohesion Policy.

Next to a strong emphasis in the overarching documents CP includes also some responses to the challenges those regions. One of the approaches is the option to modulate the co financing rates according to specific types of regions. The Regulation pinpoints the following ones:

- Island MS which are also Cohesion Countries (MT, CY).
- Mountainous areas defined according to national legislation.
- Sparsely populated (less than 50 inh./sqkm) and very sparsely populated areas (less than 8 inh./sqkm).
- Outermost regions which receive also an extra envelope within the Objective of Investment for Growth and Jobs.

Furthermore an example of a broad approach to strategies is urban areas. The Commission intends to pay more attention to urban areas. At EU level € 372 million will be dedicated to innovative urban actions that shall include studies and pilot projects to test new solutions to urban challenges that are likely to grow in the coming years. MS are obliged to foresee a minimum of 5% of ERDF to target urban areas with integrated strategies for sustainable urban development. The Integrated Territorial Investment as an option for cross-funds or cross-programme interventions has its roots in model strategies for deprived urban areas combining operations under ERDF and ESF.

At European level, cohesion can be considered as narrowing disparities between regions within the EU as a whole. Therefore also indicators such as GDP per capita, median income levels, employment rates and education levels refer to the average values of the whole EU. It is obvious that there is a different consideration of regions and indicators in the MS.

The fact that the Regulations mention specific types of regions which deserve particular attention and thus might fall under specific provisions in the implementation of CP can be considered as an important policy lever. However, the development and implementation of tailored and integrated strategies is in hands of the MS. Next to urban regions, three exemplary types of regions should be highlighted:

- Coastal regions.
- Sparsely populated, overseas regions.
- Mountainous regions.

Different regional specificities need different strategy implications that have to be met by Art. 174 (FTEU) and the EC's Green Paper on Territorial Cohesion but also by territorial cooperation programmes. Integrated strategies and multi-fund approaches that are not designed at NUTS-2 or NUTS-3 regions but at the level of individual islands or valleys as well as functional regions are able to tackle occurring problems.

The scientific debate focuses mostly on the identification of structural constraints and on barriers to development. However, strategies that would make it possible to exploit their potentials and recognise their assets remain to be defined.

Those regions which deserve particular attention due to the multi-faceted challenges and the need for integrated strategies would in principle need high governance capacities at level of LRAs. But it is evident that in particular in regions such as fragile island economies or peripheral mountainous regions the LRAs have to face significant economic constraints which usually do have repercussions on the governance capacities. For such regions the implementation of integrated strategies with a strong element of MLG is considered as the ideal policy approach but in practice is rarely found.

Particular policy options arise for LRAs in urban regions respectively for cities by fostering integrated strategies which enhance sustainable urban development. The major advantage for urban regions compared to other types of regions is that urban regions tend to have higher governance capacities partly owing to the manifold public amenities to be managed, partly owing to own statutes stemming from history. With regard to the preparation and management of programmes the implementation of integrated urban development strategies that are able to tackle multiple challenges facing their cities implies the delegation of tasks to LRAs. This might deepen the responsibility of LRAs concerning the actual implementation of integrated strategies.

### **Major challenges and trends influencing many policy areas**

Cohesion Policy has to face overarching challenges which provide new angles and have led and will lead to further impetus for policy development. These challenges are usually dominated by global driving forces, which are often beyond the control of the Member States or as the Union as a whole, yet influence the success (or failure) of the policy initiatives or responses.

The European Environment Agency, the KPMG/MOWAT report “Future State 2030” and the ASP Strategy Development Project have identified a set of all together 16 thematic fields.

This list can be enriched ad infinitum; however the set of “Major challenges and trends” seems to be adequate to the scope of the present study.

The Terms of Reference offer a useful set of categories for clustering, namely:

- Economic (crisis);
- Demographic change and migration;
- Climate change expanded by Environment
- Globalisation / External policies / Tackling of increasing geostrategic risks (with massive economic implications such as the issue of energy sources and other crucial assets).

These categories can be expanded by adding Technological and Institutional aspects.

In the table below they will be presented in a structured way (following the 16 thematic fields mentioned above) related to the implications for the Cohesion Policy and on the options available for LRAs.

The main questions to be asked in this table are:

- Is the respective global challenge and trend cluster increasing the demand/scope for a Cohesion policy intervention?
- Is the respective global challenge and trend cluster impeding the achievement of the intended benefits of the Cohesion policy intervention?
- What are the implications for LRA?

**Table 3. Major challenges and trends influencing CP and LRAs**

Category	Major Challenge and Trend	Effect on Demand/Scope of Cohesion Policy	Effect on Impact of Cohesion Policy	Implications for LRA
<u>Economy</u>	<p><i>5. A need for continued economic growth</i></p> <p><i>13. Economic interconnectedness</i></p> <p><i>16. Increased mobility of goods and persons</i></p>	<p>The pressure on enterprises and especially SMEs is growing, hence the need for specific support (e.g. administrative and tax burden, access to finance, integration in Global Value Chains) will be sustained if not reinforced.</p> <p>It will be necessary to render SMEs competitive on the global market.</p>	<p>The changes imposed by the challenges and trends are materialising much faster than the policy cycle.</p> <p>Cohesion policy can hardly react at this pace.</p> <p>At the same time a “reactive” policy can only have short term effects.</p>	<p>LRA will be exposed to competition for their movable assets and also will have to promote their territorial immovable assets.</p> <p>The provision of high-quality, stable locations are crucial although no guarantee for success.</p> <p>For that reason it will be necessary to be involved in networks and informal forms of cooperation with the business sector.</p>
<u>Demographic change and Migration</u>	<p><i>1. Diverging global population trends, with an ageing “first world”, a stabilising Asia and a rapidly growing Africa;</i></p> <p><i>2. Rapidly urbanised global population</i></p>	<p>Demographic dynamics suggest that these trends will be sustained. The demographic decline of Europe will make the integration of migrants inevitable.</p> <p>Hence the demand for employment, education and social inclusion interventions will remain.</p> <p>At the same time the administration will have to depart from static approaches and react dynamically to the needs of migrants and natives.</p>	<p>Social integration will take time to materialise. Hence the balance must be kept between short term preservation of social peace and long term integration.</p> <p>The long term nature of expected effects might lead to mid-term rejection of the policy by the electorate.</p>	<p>LRA will have to promote “grass-root” approaches and local initiatives allowing for a cost effective integration of migrants and of local community acceptance.</p>

<u>Climate Change and Environment</u>	<p><i>3.Changing disease burdens and risks of pandemics</i></p> <p><i>8. Growing pressures on ecosystems</i></p> <p><i>9.Increasingly severe consequences of climate change</i></p> <p><i>10.Increasing environmental pollution</i></p>	<p>The demand for interventions in the field of environment will be increasing.</p> <p>These will have two dimensions, one regarding hard infrastructure (e.g. sea defences or refuse incinerators) and one regarding intelligent management approaches (e.g. ecosystem management or waste prevention).</p>	<p>Hard infrastructure investments are politically more effective, since more visible.</p> <p>This could lead to a downwards spiral of reacting to hazards instead of reducing them with a steadily decreasing benefit to cost ratio.</p>	<p>LRA will have to focus on flexible operation of infrastructures (according to needs and not demand and considering territorial features and demographic trends, instead of trying to provide “one size fits all” solutions) and intensify cooperation across administrative borders.</p>
<u>Technology</u>	<p><i>4. Accelerating technological change, rise of an information society and of a knowledge economy</i></p>	<p>The demand for interventions for enhancing skills and competences and the matching of labour market needs and education/training offerings will be increased.</p> <p>Also the priorities for infrastructural endowment of regions will be affected requiring ICT and accessibility infrastructure allowing for the interconnection of knowledge hubs and the dispersion of economic activities.</p>	<p>Depending on the approach of the Cohesion policy (supporting the weaker, supporting the strong, supporting the strengths etc.) polarisation might continue.</p>	<p>LRA apart from the provision of locations will have to promote partnerships with the business sector and the society and also by attracting stakeholders via the “non-basic” sector.</p>

<u>Institutions</u>	<p><i>11. Diversifying approaches to governance.</i></p> <p><i>12. Rise of the individual</i></p> <p><i>14. Public Debt Dynamics</i></p>	<p>Cohesion Policy addresses institutional capacity and governance (1) directly e.g., through TO11, (2) indirectly (as a side effect of sectoral policies, e.g. in the context of the WFD) and (3) methodologically (through the principles of partnership, subsidiarity, multi-annual planning, evaluation etc.).</p> <p>Overall the demand for Cohesion Policy interventions will rise.</p>	<p>Impacts can be affected either by the long time needed for institutional transition and by the limitations of public debt dependency paths and austerity fixation.</p>	<p>LRA will have to further develop participative models of governance and enhance regional economic and accountability cycles.</p>
<p><u>Globalisation /</u></p> <p><u>External policies /</u></p> <p><u>Tackling of</u></p> <p><u>increasing</u></p> <p><u>geostrategic risks</u></p>	<p><i>6. Increasingly multipolar world</i></p> <p><i>7. Intensified global competition for resources</i></p> <p><i>15. Tensions on the energy market</i></p>	<p>Through the globalisation trends insecurity and volatility will increase.</p> <p>For cohesion policy interventions the focus lies on resource efficiency and energy security. Overall the demand for Cohesion Policy interventions will rise.</p>	<p>Global players might outbid the EU in the race for resources.</p> <p>Also the lack of a mechanism for securing geostrategic interests of the EU as such could render the impact of Cohesion Policy marginal.</p>	<p>LRA will have to strengthen the resilience of their regions in relation to global “shocks”.</p>

This table offers an abstract and simplified picture of the reality; in many cases global trends are positive drivers for Cohesion Policy instruments; however there are cases where global trends dwarf Cohesion Policy interventions or surpass them. For LRAs the focus is clearly on softer instruments of incentives provision and information & organisation rather than the “classical” regulative policy tools.



## **Part 2: Effectiveness, Efficiency and Governance of Cohesion Policy at regional and local level**

Cohesion policy is the only effective political device that forces different levels of government to cooperate. Therefore, not only good working institutions but also representative institutions taking into account opinions and interests of all actors involved are important for the future development of the regions.

Efficiency and effectiveness of public administrations at national, regional and local levels have a significant impact on economic development and job creation, and thus on increasing social, economic and territorial cohesion.

Likewise, the role of different actors in delivering Cohesion policy objectives as well as the modes of decision-making and public participation influence results and impact in social, economic and territorial cohesion.

Key questions to be tackled in this section are:

- mechanisms to ensure respectively to improve policy delivery across all stages of the programming / project / policy cycle (including the role of funding and financing mechanisms).
- options for CoR to provide an impetus to discussion and to strengthen the role of LRAs.

### **Mechanism to ensure respectively improve policy delivery**

The translation of strategic papers such as the Europe 2020 strategies and comprehensive guidelines into national strategies shaped by domestic policy bears the trade-off between strategic guidelines at EU level and the reality of Cohesion Policy as well as the actual use of Structural Funds at local level.

During policy coordination, the gap between the Country Specific Recommendation and national strategic and programme documents as well as the EU legislative package comprised different interpretations at national level. In fact, the regular verbal communication between Managing Authorities (MA), desk officers and different stakeholder may create misunderstandings compared to written comments although it is a necessary part in order to improve results and ensure accountability on all sides.

Vertical policy coordination from central level to LRAs in centralised MS implies difficulties as a result of information gaps and awareness with regards to each government priorities. The role of LRAs can be strengthened by national

investment strategies, territorial representatives, regional development agencies and formal agreements. In Cohesion Policy, the principle of co-financing, formalised consultation processes, dialogue platforms and informal coordination arrangements help to improve the involvement of LRAs.<sup>1</sup>

Likewise, horizontal coordination can be hindered by administrative and regulatory obstacles which can be traced back to different political-administrative systems with different individual governance and legal systems in countries and regions on both sides of a border. Consequential results can be “closure effects” for all sorts of economic, social inter-cultural or inter-personal exchange relations across EU borders<sup>2</sup>.

The European Code of Conduct on Partnership (art. 4 CPR) shall help MS organizing a meaningful partnership with relevant stakeholders. Along with already established steps such as ex ante evaluation as well as interservice consultation, the programming process shall be improved. Cross-fund investments and multi-fund programming enhanced general policy coordination and reduced the number of OPs and therefore the administrative workload.

Flexibility to design the optimal mix of actions is secured through fund-specific regulations that provide for translation of thematic objectives into investment priorities. In addition rules on thematic concentration, i.e. obligatory financial allocation and the introduction of ex ante conditionalities, bring ESIF in line with Europe 2020 and supports the development of strategic guidance in key sectors.

EU policy implementation is mostly considered as national agenda in line with the subsidiarity principle. The management structures as well as the scale and thematic content of the programme influence the number and types of actors involved in this policy stage. Likewise project assessment procedures depend on the broadness and scope of the OP as well as on the type of MS. As part of the appraisal different types of risks and uncertainty associated with public investment exist at the early stage of the investment cycle and should be re-evaluated as new information becomes available<sup>3</sup>.

MLG that can contribute to greater policy effectiveness, commitment and ownership in decision making and of policy outputs can be facilitated by regular information exchange and targeted training measures.

The moral hazard problem refers to the risk that projects with low or no added value are being implemented through ESIF programmes. Containment can be ensured through mechanism such as the building up of capacities and expertise

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<sup>1</sup> OECD 2007.

<sup>2</sup> ESPON 2013 project „GEOSPECS“.

<sup>3</sup> OECD 2014, p. 10.

in management, transparency and tangible selection criteria, analysis and guidance, MA's responsibility and quality control.

One of the most demanding tasks for most MS is the setting-up of effective and efficient control bodies which are in charge of the financial control task. The time spans from submission of payment requests to closure of control routines are often much longer than expected and prescribed<sup>4</sup>. A set of regulations for the 2014-2020 period has introduced new approaches to simplify the verification process such as standard unit costs, lump sums and flat rates. Now, MS have to take up these options and integrate it to the national eligibility rules.

Debates in policy delivery tend to focus on the absorption of funds: automatic de-commitment is perceived as one of the most significant failures for programme management. In the main partnership mechanism, the Monitoring Committee, thus the discussion of programme outcomes is clearly ranked second and often delegated to the evaluation.

Evaluation in Cohesion Policy often fails to facilitate a dialogue and mutual learning between the evaluator and the authority, project or institution to be evaluated. Pre-conditions for effective evaluations are therefore the back-up by the MA, the shared development of the key evaluation questions to be answered and the involvement of representatives from all stages of the programme cycle.

### **The role of financing and funding mechanisms**

The funds for CP (as well as those for the CAP) are tied to the economic performance of the MS. The long-term crises in the EU and the underlying options to use the funds for CP as a countercyclical investment instrument have inevitable consequences for the funding of CP. As a reaction to the economic and financial crisis in the period 2007-13, a set of specific measures for MS in economic difficulties (Stability and Growth Pact) has been introduced.

Considering that a large proportion of funding within CP goes to the less developed regions (about 50% to the regions, 20% via the CF) and assuming that the current mechanisms are being continued large-scale changes after 2020 might stem from the re-classification of the (substantial) transition regions in ES and DE and the economic developments in PL.

Lagging disbursement of funds has led to the introduction of mechanisms to ensure financial discipline such as the rule on automatic de-commitment which has immediate and substantial impact on programme management. A potentially adverse systemic impact of the de-commitment rule is that it might support a

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<sup>4</sup> In the period 2007-2013 a limit of three month has been introduced.

tendency towards standard types of projects with low degrees of implementation risks but also low potentialities to trigger off new developments.

In the period 2014-2020, particularly small LRAs in less developed regions might encounter additional disadvantages in case of programmes which do not foresee a clear ranking of projects according to needs. For them, the provision of match-funding and the capacity to pre-finance long periods until re-imbursement for operations might become even more decisive.

Any debate about the future of CP will start at the funding. Funding mechanisms can be understood as control levers of a quite sophisticated system and changes in one position will have repercussions on other system elements. Two scenarios can be imagined:

- The whole system of CP undergoes a complete change after 2020, i.e. with a substantial re-definition of all mechanisms. This is most probable in a scenario where funding is drastically reduced.
- The current system is more or less maintained and adjusted. In this case, numerous policy levers could be re-positioned such as in particular the allocation to the Funds, the distribution between types of regions (more/less developed), the co-financing rates, the advance and interim payments of the EU to MS etc.

### **Strengthening the role of LRAs**

Regions and places are increasingly considered as key level for establishing efficient policy coordination which presents a number of challenges. On the one hand, their capacities to govern EU public investment policy are strongly influenced by the differences in political-administrative systems across the EU. On the other hand they are affected by external economic and social pre-conditions such as demographic challenges and economic decline in rural areas and population growth and financial accumulation in growing urban areas.

A close cooperation between different regional and local partners in MS as well as the involvement in PA and OP development and implementation is crucial for all policy stages. A strong involvement that offers the possibility to shape policy implementation or to tailor the Investment Priority to the actual regional/local needs can be secured by the representation of MAs or Intermediate Bodies through LRAs. They can take the role of passive recipients or active policy makers – the decisive aspect of a genuine area- or place-based approach is the actual weight of the LRAs in the coordination of various policy approaches shaped by actors at national and local level. Based on literature review, the following patterns can be extracted:

Regions governing Regional OPs in countries with a long tradition of regional ESIF Programmes (DE, ES, FR, IT) benefit from the longer-term budgetary commitment for specific development goals combining funds from the EU, the national and the regional level.

On the other hand, regions governing a Regional OP in countries that experienced a decentralisation process (CZ, PL, SK), the stable longer-term funding instruments lead to a decisive shift on the capacity of self-government. In those regions, frequently financed local infrastructure is now gradually replaced by more innovation-oriented and broad types of intervention. This entails all challenges as a result of less developed intermediaries whose support of implementation in experienced regions is an important success factor.

Structural Funds policy coordination anchored at MS level implies (a) the focus on strategic issues and guidelines to support the pace of implementation and (b) the lack of options and communication routines for a regular exchange between the operative units. Here, it might be wise to involve LRAs in inter-ministerial committees linking sectoral ministries that coordinate ESIF at national level in order to improve operative management of the programmes. In countries where no such committees exist a strong involvement in the Monitoring Committees as coordination mechanism of ESIF is recommended.

Moreover, the capacity for project development and co-funding – the governance capacity at local level – might be decisive for the success in the acquisition of projects often regardless of the actual needs. The introduction and implementation of the strategic CLLD and ITIs shall meet coordination and territorial challenges more sufficiently in the future.

However, the weak involvements of local authorities in the programming process as well as their weak representation in the partnerships reinforce their low governance capacities and capacities in project implementation. Overall, the adaptability of institutions and collective learning processes are still dependent on the institutional architecture at national level and it should be tackled by helping the MS and various partners to build their own strategy. The focus can be on public innovation policies as trainings on “assessment risks”.

From the structural perspective, implementation rules should be simplified and the current bureaucracy must be reduced through innovative approaches and improvement of internal and external communication channels.

The place-based approach facilitates the mobilisation of stakeholders (including private sector) and their specific territorial knowledge. Thus, the compatibility between pan-European overarching objectives and the territorial realities can be

improved<sup>5</sup>. In addition, the linkage of policy decisions and the peoples' perspective must be increased by linking effectiveness and democracy, transparency and bottom-up approaches.

In order to identify the challenges of each territory and help defining strategic goals of a specific region in relation to EU policy a territorial approach of foresight could be followed. The relationship between the finances of the Cohesion Policy and the sub-national budgets, including the Stability Pact provision has to be tackled.

In relation to EU funding eligibility, conditionalities that increase the regional policy in the MS could be an instrument to meet regional needs. Moreover, it might be worth considering the creation of a single EU mono-Fund that supports regions according to its specific needs and challenges.

Also the advantages and disadvantages of central vs. decentralised implementation of sectoral vs. integrated programmes are of high importance when arguing for more sub-national support.

The impact in the real economy which are still difficult to measure should be tackled by considering the role of different actors in delivering Cohesion policy objectives through projects' results as well as the modes of decision-making and public participation. Moreover, models of partnership and MLG decision-making have to be considered asking for the different results, the level and leverage of co-financing as well as its providing authority or institution and amount.

The implementation of a proportional audit system based on a new partnership approach and on the MLG principle is something to be elaborated. A future evaluation system should be based on more suitable indicators and the effectiveness has to be linked to a result-oriented approach.

With regards to accountability, transparency and result-orientation, the promotion of further exchange of best practice and concrete cases among regions is of great importance.

In order to overcome the sharp economic divide between regions across Europe LRAs must be adequately involved in the design and the delivery of the national responses to the strategic framework of the EU for the forthcoming period. This will follow established routines in countries with long-standing tradition of regional self-governance but it constitutes a significant challenge for some of the new MS, where the involvement of regional bodies still is in a fairly early

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<sup>5</sup> Böhme et al. 2013.

stadium or no self-governing regions exist. In the latter case the strategic gap between national policy objectives and local interventions might be even wider. These points at the need that national level and the EU – in particular DG Regio – provide pro-active guidance in the translation of strategies into action at LRA level. It is evident that the closer the administrative tier is ‘to the ground’, i.e. to the everyday life of citizens, the stronger the need for pragmatic approaches. On the other hand there is a need to show a broader variety of options to stakeholders at local and regional level in order to avoid the widespread duplication of similar local policy responses<sup>6</sup>.

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<sup>6</sup> cf. Metis 2011, The complementarity of national and Community interventions aimed at reducing disparities in economic and social development, Commissioned by Committee of the Regions, DTC Unit 4.





# 1 Introduction

The study series on the Future of Cohesion policy aims to provide a new impetus to the work of the Committee of the Regions (CoR) and its members in the policy debates on the efficiency and effectiveness of Cohesion policy (CP) from the perspective of local and regional authorities (LRA). In this light, the main research topic is Cohesion policy beyond 2020. The specific objectives of the present study and the study series are:

- Defining a research methodology as well as the main topics to be analysed in the file note and the subsequent Reports I and II;
- Addressing a number of fundamental questions and issues related to Cohesion policy as highlighted in the upcoming seminars;
- Bringing a strong regional and CoR perspective into the discussion at an early stage.

The methodology was first outlined in the file note from March 2015 and it has slightly been adapted in the present report. This paper is the first one out of two requested reports, which follow different scopes:

- Report 1 aims to outline the trends and major aspects of effectiveness, efficiency and governance related to Cohesion policy from the perspective of LRAs.
- Report 2 aims to present models and ideas for the future of Cohesion policy.

The broad range of topics addressed in the Terms of References for this research assignment reflects how wide the range of the Cohesion policy debates is.

The specificity of this assignment consists in reflecting the position and the role of the LRAs throughout all of the research steps. Given the broad character of Cohesion policy, the approach of the study team is to produce concise and structured analysis reports.

The planned reports and seminars are considered to be a vehicle and an incentive to intensify the policy debate between the key Cohesion policy actors and the representatives of LRAs.

Furthermore, in the course of preparing the present report, the Metis GmbH team used state-of-the-art information on Cohesion policy in Europe, including the main relevant publications of the European Commission's DG Regio. This essential approach will be used for the upcoming reports as well.

To some extent, this research follows the sixth Cohesion Report<sup>7</sup> of the European Commission. Throughout the report there has been made reference to the sixth Cohesion Report where necessary and needed. Furthermore, it follows the CoR's recommendation of including information from the existing and the planned studies mainly from the European Commission, the European Parliament and think tanks, in order to ensure complementarity with the latest research. More specifically, the following sources were taken into account drafting this study:

A main source of information were the studies of the European Parliament (EP) in the field of regional policy, most notably the 2013 Study on "SMEs in the Cohesion Policy Management Cycle" prepared by the Centre for Industrial Studies (CSIL)<sup>8</sup> as well as a 2012 study on EU agriculture<sup>9</sup> mainly feeding into the respective Chapters 2.1.1. on "Agriculture and Forestry" and 2.2.6 on "SME Policy" as well as the analysis of the policy cycle. The Authors themselves had been involved in several of the EP studies<sup>10</sup>, thus ensuring a flow of information.

Studies commissioned by the European Commission, DG REGIO provided valuable input to the Study, most notably:

- Böhme et al., Study on promoting multi-level governance in support of Europe 2020, Inception Report, European Commission Regional and Urban Policy, 2013.
- London School of Economics (LSE), Study on the Impact of the Single Market on Cohesion: Implications for Cohesion Policy, Growth and Competitiveness, Study commissioned by DG Regio, London 2011.

The results of two recent publications of DG REGIO providing a broad overview of policy issues were used throughout the Study:

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<sup>7</sup> European Commission, Investment for jobs and growth. Promoting development and good governance in EU regions and cities. Sixth Report on economic, social and territorial cohesion, Brussels, July 2014

<sup>8</sup> Centre for Industrial Studies (CSIL), Public Policy and Management Institute (PPMI), SMEs in the Cohesion Policy Management Cycle, Study commissioned by the European Parliament, Directorate General for Internal Policies, Policy Department B – Regional Policies, Brussels, 2013.

<sup>9</sup> European Parliament/Directorate General for Internal Policies Policy Department B: Structural and Cohesion Policies Agriculture, How to improve the sustainable competitiveness and innovation of the EU agricultural sector, Brussels 2012.

<sup>10</sup> Metis GmbH, Public procurement and Cohesion Policy, Vienna 2012.

Metis GmbH, EPRC, An assessment of multilevel governance in Cohesion Policy 2007-2013, Vienna 2013.

Metis, GmbH, Implementation of Cohesion Policy 2014-2020: Preparation and administrative capacity of Member States, European Parliament Policy Department B: structural and cohesion policies, Vienna 2014.

- Van den Brande, L., Multilevel Governance and Partnership - The Van den Brande Report - Prepared at the request of the Commissioner for Regional and Urban Policy Johannes Hahn, October 2014.
- Papers presented at the conference "EU Cohesion Policy 2014-2020: An academic and policy debate" organised by DG REGIO in Riga on 4-6 February 2015.

In respect to the chapter “Analysis of the policy cycle and the different approaches”, the upcoming studies carried out by the European Commission, DG REGIO, assessing the new elements introduced to the programming cycle will provide additional empirical evidence testing the hypotheses put forward by the Authors (see the below table). The studies have a twofold function, on the one hand side collecting evidence for the new reporting scheme required and on the other hand side serving as a basis for policy design for the period after 2020.

**Table 4. DG REGIO studies upcoming or underway**

Topic	Status	Comments
<i>Studies on the integration of new regulatory elements in the programming process carried out by the European Commission, DG REGIO</i>		
Study on the use of new provisions during the programming phase of the European Structural and Investment (ESI) Funds	ongoing	Own reflections on this issue can be found in the table in Chapter 2.1
Study on the implementation of the provisions in relation to the ex-ante conditionalities during the programming phase of the European Structural and Investment (ESI) Funds;	ongoing (prepared by Metis)	Results of Interim Report used for Chapter 3.1 “Analysis of the policy cycle and the different approaches”.
Study on the implementation of the provisions in relation to the performance framework during the programming phase of the European Structural and Investment (ESI) Funds;	ongoing	The topic seems less relevant for the key objectives of the study since the performance framework is generally understood as one of several instruments aiming at better financial discipline in programme implementation – see Section 3.3 on financing
Study on the implementation of the partnership principle and multi-level governance during the programming phase of the European Structural and Investment (ESI) Funds;	ongoing	The contractor has undertaken also research work on the issue of the Partnership Principle for the European Parliament and our view on the subject is quite controversial as can be seen in our major statements in Section 3.
Study on setting up a database to assess impacts and effects of certain thresholds and limits in Regulation (EU) No 1303/20131 (CPR).	ongoing	Most interesting new perspective might come from the more detailed analysis of revenue-generating projects.

<i>Studies foreseen by the European Commission, DG REGIO, for 2015</i>		
Study on simplification, administrative burden and administrative costs;	foreseen	Key issue; it is intended to run interviews with SIF-practitioners on this pressing issue in the interview phase
Study on alternative delivery modes	foreseen	For the time being we could not find any detailed information on the scope of the study.
Feasibility study on performance based budget support including legal set-up	foreseen	For the time being we could not find any detailed information on the scope of the study.
Study on coordination and harmonisation of the ESI funds and other EU instruments	foreseen	For the time being we could not find any detailed information on the scope of the study.
Study on application of new implementation mechanisms by Member States	foreseen	For the time being we could not find any detailed information on the scope of the study.
Study on improving the take up and effectiveness of financial instruments	foreseen	Metis is currently working on the topic of financial instruments. The fundamental potentialities have been highlighted in Section 2 as well as in the chapter on SME policy.
Study on linkage with Country Specific Recommendations and supporting structural reforms	foreseen	Close link to the assignment which just started for the CoR – the Authors expect to be able to use some of the results also as input for this study

## Methodology

The methodological approach taken for the present report has allowed for balancing between the following elements:

- setting the scene for future Cohesion policy, i.e. outlining major trends and challenges and their impact at regional and local level,
- developping a comprehensive review of the policy delivery chain starting from the current mechanism for the distribution of European Structural and Investment Funds (ESIF) among the Member States to the challenges related to implementation. It therefore draws an outline of the key factors determining the efficiency and effectiveness of Cohesion policy; in short, the governance process.

The research in the above-mentioned fields moreover builds a basis for the next steps of the study series on the future of Cohesion policy. For this subsequent “Report 2” to be delivered by the end of 2015, the following points will be crucial:

- the explicit and implicit role of key indicators for the definition of goals, as well as a review of the debate on goals and conflicts of goals,
- a synergetic view on the underlying models and policy choices which places future EU Cohesion policy in the context of other EU policies (in particular Horizon 2020, Europe 2020, Common Agricultural Policy – CAP).

For part 1 of Report 1, it was important to **capture the field of Cohesion policy** in the European Union. Cohesion policy is multi-faceted, driven by many goals and has ample ramifications in many policy areas: in short, it cannot be captured and contained in the debate of one or two key policy dimensions. In the words of the European Commission:

*“The new Cohesion policy 2014-2020 means regions and Member States must target EU investments on four key areas for economic growth and job creation: Research and Innovation, Information and Communication Technologies (ICT), enhancing the competitiveness of small and medium-sized enterprises (SMEs) as well as supporting the shift towards a low-carbon economy.”*<sup>11</sup>

The underlying challenge for the research was – and will be for the next steps – to develop an approach that supports the diversity of the debate, but at the same time ensures that crucial points are not neglected.

In view of capturing Cohesion policy and getting a picture of the gaps, trends and challenges, the **first step** consisted in outlining the major trends expected in the three traditional sectors:

- Agriculture and Forestry.
- Manufacturing and Industries.
- Service sector.

This included an analysis of the visible as well as the expected major territorial implications of the developments within those three sectors.

Besides exploring the driving factors for the economic, environmental and territorial challenges for each sector, a table has been developed to highlight the challenges and trends beyond 2020 for social, economic and territorial cohesion. The perspective of the local and regional authorities also has been tackled in each of the sectors.

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<sup>11</sup> EU Cohesion Policy 2014-2020, Targeting Investments on Key Growth Priorities. [http://ec.europa.eu/regional\\_policy/sources/docgener/informat/2014/fiche\\_innovation\\_en.pdf](http://ec.europa.eu/regional_policy/sources/docgener/informat/2014/fiche_innovation_en.pdf).

**Template table: Challenges and trends for the three sectors beyond 2020**

	Social Cohesion	Economic Cohesion	Territorial Cohesion
Change of paradigms in each policy			
Growing interdependences			
Role of labour			
Price development for energy and inputs			
Role of European networks			
Developments in STI			
Role of regulatory Policies			
Role of the Single Market			
<b>Perspective of LRAs</b>			
Regulatory acts			
Incentives			
Information and Motivation			

The **second step** taken to capture Cohesion policy consisted in reviewing the key sectoral policies that are closely interlinked with Cohesion policy. These sectoral policies are:

- Environment, climate change adaptation, low-carbon economy and resource efficiency.
- Labour market and social policies, health care.
- Education and qualification.
- Research and Innovation.
- Network development and infrastructure.
- SME policy.

It is important for the whole report and the succeeding deliverables to limit the number of policies discussed, in order to develop not only a comprehensive but also a readable report. The approach above is a rough cluster that pools together policy areas which follow similar development logics<sup>12</sup>.

The **third step** taken to draw a picture of the status quo of Cohesion policy in Europe consisted in giving some thought to specific regions in Europe. Despite the apparent dominance of sectoral approaches, the aspect of policy focus given to specific regions must not be forgotten. In parts, the EU provisions for Cohesion policy do foresee or shape incentives in that way. Some Member

<sup>12</sup> The clustering was done in cooperation with the Committee of the Regions and has been approved before the drafting of this paper started.

States already use such approaches, which are then reinforced by EU Cohesion policy.

Finally, the **fourth step** in part 1 of the present Report 1 consisted in analysing the trends and challenges influencing several policy areas (so-called ‘mega-trends’). Cohesion policy has to face overarching challenges which offer new angles and which have and will lead to further impetus for policy development. These challenges are usually dominated by global driving forces, which are often beyond the control of the Member States or as the EU as a whole. Yet, they influence the success (or the failure) of the policy initiatives or responses:

- The economic and financial crisis.
- Demographic change and migration.
- Climate change.
- Globalisation / External policies / Tackling of increasing geostrategic risks (with massive economic implications, not least with respect to the energy resources and other crucial assets).

The implications for Cohesion policy are categorised either as synergetic, detrimental or indifferent. Similarly, the implications on the options available for LRAs are categorised in a structured manner, namely by the possible instruments as defined in the section “Analysis and review of sectoral developments and the related territorial implications”, i.e. regulatory acts, incentives and information and organisation.

Part 2 “**Effectiveness, Efficiency and Governance of Cohesion policy at regional and local level**” of Report 1 tackles the issues related to **implementation**. Cohesion policy is the only effective political device that forces different levels of government to cooperate. This points to the importance of well-functioning and representative institutions that take into account the opinions and the interests of all actors involved, not least for the future development of the regions.

The efficiency and effectiveness of public administrations at national, regional and local levels have a significant impact on economic development and job creation, and thus on increasing social, economic and territorial cohesion.

Likewise, the role of different actors involved in the implementation of Cohesion policy objectives as well as the modes of decision-making and public participation influence the results and the impact on social, economic and territorial cohesion.

The key issues to be tackled in this section are:

- the mechanisms that aim to ensure that policy delivery is improved across all stages of the programming / project / policy cycle;
- the possible options for the CoR to provide an impetus to relevant discussions and to strengthen the role of LRAs.

Furthermore, the report analyses the differences between decentralised countries (e.g. Germany, Austria) and countries with rather centralised systems (the Czech Republic, Poland) which used integrated Regional Operational Programmes in the 2007-2013 programming period.



## **2 Gaps, trends and challenges with impact at regional and local level**

Following the order form this component shall analyse:

- challenges at LRA level linked to the impact of the crisis and a long period of low economic and employment performance;
- the regional and local impact of major trends impacting economic, social and territorial cohesion and challenges of the growing economic, social and territorial divide;
- the challenges for LRA authorities arising from the trend towards centralisation of EU economic and monetary policies.

### **2.1 Analysis and review of sectoral developments and the related territorial implications**

This part serves to set the scene for the subsequent part of the report which is focussed on implementation. The intent is to briefly review:

- trends and challenges from a sectorial perspective,
- the major territorial implications and thus the major challenges for LRAs,
- the implications for Cohesion Policy,

The structure of the ESIF is still markedly oriented on economic sectors, thus it is proposed – as a point of departure - to outline the major expectable trends in the three traditional sectors and the visible as well as expectable major territorial implications of these developments:

- Agriculture and Forestry.
- Manufacturing and Industries.
- Service sector.

#### **2.1.1 Agriculture and Forestry**

Agriculture has experienced a substantial transformation in Europe in the post war era transitioning from small scale, semi-subsistence family farm management to industrialised and specialised holdings with a wide intensification of the use of intermediate inputs and exploitation of resources. However, “pockets” of traditional farming still exist and are predominant in

some countries, especially in the periphery and in some eastern European countries, as a result of restitution processes. These small holdings are under pressure from large play-makers and need protection, since they pose a sustainable, grass-root form of cultivation. Their importance has been increasingly repeatedly stressed for the viability of rural areas.

This transformation was not void of side effects on environment (affecting landscapes, habitats, water bodies and soils), socioeconomic situation (leading to market integration, increased incomes and social advancement but also to polarisation, increase of inequalities, outmigration and greater inter-dependencies) and territorial structures (high demand in well endowed areas and to marginalisation and abandonment in less favoured and peripheral regions).

The Common Agricultural Policy (CAP), one of the main issues of the Treaty of Rome, has significantly contributed to this transformation through the aims defined in Article 38 regarding competitiveness, agricultural productivity by promoting technical progress, the optimum utilisation of production factors, income increase for a fair standard of living and assurance of the market stabilisation and availability of supplies at an affordable price.

In the frame of the Agenda 2000 the CAP has reoriented itself by becoming more integrative and addressing rural development on a broader base than in the past. This is not always consistently followed; funds for rural development were reduced while at the same time the scope broadened. Furthermore, *“although cohesion is not an explicit goal of the CAP, it is intended to take account of ‘the particular nature of agricultural activity, which results from the social structure of agriculture and from structural and natural disparities between the various agricultural regions. Its aim is to ensure economic and social progress in agriculture and rural areas while providing support for the supply of reasonably-priced food to EU consumers.’”*<sup>13</sup>

The approach of the CAP in 2014-2020 attempts to pay tribute to the multi-functional nature of European agriculture departs from plain producer support to a broader approach encompassing food security, environmental sustainability, climate change consideration and resilience as well as territorial balance.

At the same time on global scale the agricultural sector faces challenges, many of which are driven by factors that are external to agriculture. These can be clustered as:

- economic challenges driven by globalisation, rising demand for certain crops and products caused by growing population and changing

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<sup>13</sup> Sixth Cohesion Report, p. 188 (see also Treaty of the Functioning of the European Union, Article 39(2) on CAP.

consumption preferences and patterns, pressures on production costs due to high input costs and the deteriorating position of farmers in the food supply chain, a declining rate of productivity growth, extreme environmental effects driven by local and global processes, ensuing price volatility due to production disruptions on the one hand and speculation on the other. These elements along with the WTO process of liberalisation of international trade lead to systemic instability of agricultural markets;

- environmental challenges driven by global (e.g. climate change) and local processes (e.g. due to the overexploitation of local resources like soil and water, nutrient emissions, destruction of landscapes and habitats and threatening biodiversity through monocultures). Agricultural production contributes to greenhouse gas (GHG) emissions, via methane produced by livestock and emissions from agricultural soils. The environmental pressures are accentuated by the dominating economic imperatives described above and by the demand for resource intensive cultures and output-maximising species. The long-term sustainability of agriculture and the ability of agro-ecosystems to provide services beyond food production is being undermined by environmentally-harmful farming practices. While in Europe environmental pressures are reduced, these trends are continuing globally. Even in Europe however, where emissions are declining, former loads lead to “diffuse pollution”. At the same time policy makers underline that agriculture is increasingly important in delivering public environmental goods and in delivering ecologically sustainable products; to what extent this is achieved is debatable due to path dependencies and so called rebound effects;
- and territorial challenges of rural areas in relation to demographic, economic and social developments including marginalisation, depopulation, natural reforestation as well as polarisation and relocation of businesses on the one hand but also emergence of alternative employment opportunities and increasing land demand for non-agricultural purposes like leisure, retail and housing, especially in the vicinity of urban areas or eventually for hoarding farm land instead of using it.

**Table 5. Challenges and trends for agriculture beyond 2020**

	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Change of paradigms in agricultural policy	Growing importance of diversification of production and job opportunities	WTO driven market liberalisation and international trade Integration of long-term sustainability Compensation schemes for environmental goods	Adoption of area-based approaches
Growing interdependences	Local livelihoods threatened by global economic and environmental processes	Increasing demand for capital investments and credits Integration in supply chains	Need to exploit location advantages regarding conditions and proximity to markets
Role of labour		Growing importance of non-resident low wage/low skills labour due to the global competitiveness pressure	Outmigration of skilled labour
Price development for energy and inputs	Marginalisation of holdings with less investment potential	Pressure for cost reduction, output maximisation and negligence of externalities	Marginalisation and abandonment of less favoured areas
Role of European networks	Social Innovation	Innovation	Good practices
Developments in STI	Alternative sources of employment	Precision agriculture	Connectivity and reduction of remoteness
Role of regulatory Policies	Social standards	Introduction of standards	Infrastructure endowment
Role of the Single Market		Competition	Marginalisation and diversification
<b>Perspective of LRAs</b>			
Regulatory acts		Definition of permits, conditions etc. for economic operation	Land use definitions and restrictions
Incentives	Provision of infrastructure Social innovation	Competition for business location Fiscal incentives	Provision of infrastructure Fiscal incentives
Information and Motivation	Social innovation	Marketing	Branding

## 2.1.2 Manufacturing and Industries

Crucial point of the industrial transformation is the integration of firms into GVCs with an increasing division of labour. Regulatory policies fostering standardisation additionally support modularisation in industries. The single market favours intra-EU industrial trade. There is an inherent tendency to foster concentration in production and trade. Higher mobility of firms increases the importance of regional competitiveness. Proximity to transport, energy and telecommunications hubs is of paramount importance. Enabling technologies such as ICT play a key role.

The growing share of services in VA generation leads to manufacturing becoming closely intertwined with services. An integrated view on services and manufacturing is required also leading to a shift of the policy focus to aspects of the new manufacturing era like the rising role of S&T. The traditional industrial worker is replaced by different types of job profiles with higher requirements for qualified jobs (e.g. communication and IT skills). The overall result is a tendency towards regional concentration due to higher likelihood of location spill-overs and availability of staff.

The challenges the industrial sector faces from these trends can be clustered as:

- economic challenges driven by globalisation: The global competition puts European industry in a difficult position concerning its energy and raw material supply since prices are high and dependency on imports is high, increasing the risk of deindustrialisation. The TEN play a key role here, especially for regions that are not located in close proximity to the main hubs. The crucial role of MNEs in RTDI poses challenges for national policies, in particular for smaller countries.
- social challenges, directly and indirectly caused by the economic trends. The changes in job profiles foster segregation on the labour market – on the one hand highly skilled workers, on the other hand jobs with low skill requirements and often even precarious working conditions; in turn resulting in a need for new models in education with stronger emphasis on practical skills. Growing need for continuous training and skills development of the work force. The risk of de-industrialisation is a key argument in the political debate of social partners about wage developments in industries. Commuting and job migration, also across Europe, increase. Change of social fabric in communities in case of considerable shares of in-migration; adverse consequences in case of massive out-migration (e.g. problems to maintain basic services). There is a strong need of modernisation of the public sector and new models of governance in order to cope with the new requirements, often meeting

resistance. Global tax optimisation strategies of MNEs imply the risk of tax erosion with a subsequent risk for public spending on social issues. Agglomeration tendencies around global innovation hotspots may largen the cultural and social divide.

- territorial challenges: increasingly difficult position for peripheral rural areas (derelict ageing communities where major parts of labour force out-migrate or commute) resulting in a tendency towards concentration and agglomeration. In case of de-industrialisation job losses and massive consequences at level of LRAs (triggering vicious circles). Tendency of segregation in urban areas; emergence of poverty pockets fosters further out-migration. Investment strategies for energy islands are crucial for location competitiveness. Local acceptance of large-scale infrastructure and environmental concerns have become a sensitive issue (which in turn increase cost of development and construction).Increasing cost for site development with uncoordinated site development fostering urban sprawl and massive increase of motorised transport. In case of de-industrialisation derelict industrial sites; environmental risks, need for expensive works in site rehabilitation.

**Table 6. Challenges and trends in Industries and manufacturing beyond 2020**

	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Change of paradigms in industrial policy	Global tax optimisation strategies of MNEs with risk for public spending on social issues	Integration of firms into GVCs, rising role of S&T, fusion of manufacturing and services	Global strategies of enterprises altering perception of location factors; increasing division of labour along GVCs
Growing interdependences	Changes in skill requirements, polarisation, job migration	Growing share of services in VA generation	Tendency towards concentration
Role of labour	Segregation on the labour market	Higher requirements for qualified jobs, need for new models in education	Commuting and job migration, difficult position for peripheral rural areas
Price development for energy and inputs	Risk of de-industrialisation as key argument in wage negotiations	Difficult competitive position of Europe(high prices, dependency on imports)	In some cases minor advantages for certain locations close to hubs due to lower transport prices for transportation

	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Role of European networks		Important for competition and price developments in transportation, energy and ICT	Investment strategies for energy islands; local acceptance of large-scale infrastructure
Developments in STI	Agglomeration tendencies largen cultural and social divide	Challenges for national innovation policies in smaller countries due to role of MNEs	Agglomeration tendencies – fostering local knowledge spill-overs Key role of enabling technologies such as ICT
Role of regulatory policies	Need for new models of governance (meeting often a strong resistance)	Economic implications (e.g. standardisation, Intellectual Property and patenting)	Diversified business environment in terms of national regulatory policies – for some industries an important location factor
Role of the Single Market		Market integration favours intra-EU industrial trade; increasing competition; concentration in production and trade	
<b>Perspective of LRAs</b>			
Regulatory acts		Definition of permits, conditions etc. for economic operation	Land use definitions and restrictions
Incentives	Provision of attractive education infrastructure	Competition for business location Fiscal incentives	Provision of infrastructure Contribution to investment in facilities Fiscal incentives
Information and Motivation	Strategies to attract training and education facilities	Location marketing	Branding

Source: OECD, 2014, EC 2014, own considerations.

### 2.1.3 Service sector

*“The service sector produces “intangible” goods, some well-known—government, health, education—and some quite new—modern communications, information, and business services.”*<sup>14</sup>

In recent decades, there has been a notable move of labour mainly from the industrial sector but also from the agriculture sector to the service sector within the EU. This process of “tertiarisation” resulted in the fact that the service sector is now the main source of employment in all of the EU countries. In 2011, almost 70% of the workers in the EU carried out their functions within the tertiary sector. The services sector also accounts for some three-quarters of the EU’s GDP.

It should be noted however that while the countries of the south of Europe now have comparable levels of employment in the service sectors with the northern EU countries, the countries that have joined the EU in its most recent waves of enlargement have a lower level of tertiarisation.

The increased tertiarisation in the last decades in Europe can be explained by the following factors:

- The increase in the standard of living in Europe has resulted in a stronger demand for cultural, tourism, leisure and health services.
- The development of the welfare state insinuates the provision of specialised services.
- The delocalisation of European companies: the companies manufacture their products outside the EU but carry out the service activities (advertising, design, technical assessment, customer service, etc.) within their countries of origin.
- More complex production processes requiring more intermediates. This transformation however did not come without any side effects. First there are positive effects on the environment in the countries where the companies are based. Producing services tends to require relatively less natural capital and more human capital than producing agricultural or industrial goods. Another benefit of the growing service sector is that by using fewer natural resources than agriculture or industry, it puts less pressure on the local, regional, and global environment.

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<sup>14</sup> World Bank, Growth of the Service Sector, p. 52.



## **Society**

The increased tertiarisation had the following effects on society:

- Demand has grown for more educated workers, prompting countries to invest more in education—an overall benefit to their people.
- The distribution in the society is changing gradually. As a result of the increased labour force in the services sector, the working conditions of the employees have become unequal (long hours, little work/life balance, unequal distribution of wages) with more precarious jobs and the growing phenomenon of the “working poor”. This will influence the policy-measures to be taken in the next decades, which have already started now with ideas such as corporate social responsibility (CSR) and flexible working conditions.
- The demographic challenges faced in Europe and the consequent needs (ageing society with a rapidly growing proportion of people aged over 65 and over 80; fewer children / woman; the increase of female employment in the past decades; immigration) change the landscape yet again and will influence the shape of the services sector in the next decades (growing demand for social care services, growing demand for childcare, etc.)
- Immigration has increased to generally fill the gaps in the labour markets; the integration has to be ensured through more adequate policy measures (educational measures, job placements, coaching, etc.).

## **Economy**

The increased tertiarisation had the following main effects on the economy:

- Services sector will remain the main source of income and employment in Europe; territorial cohesion will result in similar levels of tertiarisation across the EU countries.
- New jobs and new employment models will be created based on the needs of the economy:
  - Innovative services, new jobs to be created in innovative economy given that even manufactured goods require service such as customers services and technical support which needs to be adequately educated (ICT, finance, ...).

- Services will continue to move towards high-end/ luxury services as the costs are decreasing (economies of chain) partly due to a trend towards a declining middle-class.

■ Immigration should be seen as valuable additional resources by policy-makers; educational and integration measures should be further promoted in view of ensuring that the resources and skills are used as effectively as possible to meet the societal and economic needs.

**Table 7. Challenges and trends for services beyond 2020**

	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Change of paradigms in services	Services will keep on growing but change in structure and focus based on demographic changes, to specific target groups (active ageing, healthcare, childcare, integration of migrants)	More economic cohesion across EU MS and within the MS due to an increasing tertiarisation which is unlikely to stop.	More territorial cohesion due to tertiarisation across the EU and within its MS. Demographic change, need for more social care and services
Growing interdependences	New types of services (esp. social services and healthcare) increasingly needed due to demographic changes (ageing society, immigration) and changing demand through loss of middle-class (more luxury and high-end services)	Increasing demand for innovative services (ICT, finance) and, on the other hand, social workers due to demographic changes	Different impact of economic and demographic changes on rural and urban areas; Therefore different needs in terms of services; however, services will increase territorial cohesion through their growing demand everywhere
Role of labour	Skilled labour force needed in services: Innovative service sectors (ICT, finance) on the one hand, and social services on the other hand, particularly for elderly care (new skills for new jobs; skilled labour migration)	Need for skilled labour for specialised and innovative services such as ICT and need for labour force in filling job gaps in social care (e.g. older people in the context of an ageing society)	Outmigration of young people, brain drain need to use the resources coming from the skilled labour migrants in a way to accommodate the different needs and ensure territorial cohesion

	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Price development for energy and inputs	Savings by increasing services, e.g. in RD	Less consumption	Advantage for regions with renewables
Role of European networks	Social and economic/ technological Innovation; good practices on how to use labour force for current needs	Innovation/ exchange of knowledge and experiences with innovative services; exchange of job placements	Good practices
Developments in STI	Demand for research	skilled workers	Territorial concentrations (research regions) but also possible for remote services
Role of regulatory policies	Social standards based on the fact that the challenges and needs faced are similar across the EU-28 (focus on education: new skills for new jobs, to ensure the labour force is fit for the present and future services sector)	Introduction of standards, ensuring fair competition with the growing demand and supply of innovative services	Ensuring the needs in different territorial areas are covered when the services sector spreads out even more to all administrative levels and changes due to a growing modern economy
Role of the Single Market	Infrastructure to support employees concerned in the changes in the social services sector (education, social infrastructure)	Fair competition, exchange of knowhow and experience on the impact of an innovative economy and demographic changes on the services sector	Ensuring an adequately skilled labour force (e.g. through mobility incentives) and infrastructure so that the needs in different territorial areas are covered
<b>Perspective of LRAs</b>			
Regulatory acts	Stronger focus on services of all kinds (innovative / social), depending on competencies	Focus on fair competition and corporate social responsibility to ensure social justice in the context of economic and societal changes	Ensuring territorial cohesion and a fair access to all kinds of services; stronger focus on social services also within the EU MS

	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Incentives	Adapting skills to improve services, Encourage the increase of relevant services based on current demographic trends, Ensuring the provision of adequate infrastructure; Ensure corporate social responsibility and flexibility to reduce the working poor phenomenon	Fair competition of services once offers are diversified, Adequately skilled labour competition, Fair and adequate working conditions and wages across types of services	Exchange of practices, Skills transfer and labour transfer between rural and urban areas, Territorial aspects of infrastructure needed
Information and Motivation	Social innovation		

## 2.2 Review of major sectorial policies

The review of the sectorial developments in the chapter above will be combined with a review of trends and territorial implications in key sectorial policies which are closely interlinked with Cohesion Policy. These are:

- Environment, climate change adaptation, low-carbon economy and resource efficiency.
- Labour market and social policies, health care.
- Education and qualification.
- Research and Innovation.
- Network development and infrastructure.
- SME policy.

It is important for the whole report and the following papers for the future of CP to limit the number of policies being discussed since the intent is providing a comprehensive albeit readable document. The approach above is a rough clustering where policy areas which follow similar development logics have been pooled<sup>15</sup>. The table below shows the rationale behind these clustering efforts.

<sup>15</sup> The clustering was done in cooperation with the Committee of the Regions and has been approved before the drafting of this paper started.

**Table 8. Rationale for the chosen approach to clustering of sectorial policies**

<b>Policy</b>	<b>Element of clustering</b>	<b>Funds* and IPs</b>
Environment, climate change adaptation, low-carbon economy and resource efficiency	Waste and water management are key items in CP of EU 12/13 – this type of infrastructure accounts for major shares of funding in CP Major aspects of resource efficiency and climate change adaptation: renewable energy, low carbon economy Disaster resilience: flood prevention, measures in mountainous areas,	CF and ERDF TO 4, 5 and 6 6 [excl. 6g)] IP 4a)
Labour market and social policies, health care	Established policy, in most MS clear-cut responsibility of line ministries	ESF, (ERDF) ESF – Art. 3.1a),b) ERDF - IP 8d) ERDF - TO 9a),b),c)
Education and qualification	Established policy, in most MS clear-cut responsibility of line ministries	ESF, ERDF ERDF - TO 10 ESF – Art. 3.1c)
Research and Innovation	Clustering of policies and sectorial approaches where development is mainly driven by technology development (driven by the interplay of public and private sector from fundamental research to industrial development); Energy use and efficiency is a key driver in technology development (e-mobility, buildings etc.)	ERDF TO 1 IP 4b),c), d), e), f), g) 6g) ESF – Art. 3.2a),b)
Network development and infrastructure	Transport, energy, ICT – pre-condition to make things happen; European (TEN), national, regional and local dimension; comparable planning logic and implementation across the sectors (planning and financing, options for PPP, need for EIA, challenges of public acceptance at level of LRAs etc.)	CF and ERDF IP 2a) TO 7
SME policy	Key issue of access to financing, option for financing instruments (e.g. risk capital), strengthening new firm foundation and job creation through mixed bundles of actions	ERDF, (ESF) ERDF - IP 2b) ERDF - TO 3 ESF – Art 3.1a)iii) ESF – Art. 3.2d)

Source: own considerations.

\* Codes according to ERDF and ESF Regulations.

In the following the clustered sectorial policies are described in detail giving an overview on the status quo in Europe.

## **2.2.1 Environment, climate change adaption, low carbon economy and resource efficiency**

### **Water**

The availability of water in the necessary quantity and quality is a *conditio sine qua non* for any kind of activity. Water resources are under continuing pressure in the entire world and in Europe; pressures range from contamination, exaggerated extraction and volatile availability due to, inter alia, climate change.

#### Major trends in a nutshell

Protecting water resources and ensuring qualitative and quantitative availability is a cornerstone of EU environmental policy. The Water Framework Directive 2000/60/EC (WFD) is a milestone in this protection effort indicating a turn from sectoral approaches (e.g. on protection of drinking water, on quality of bathing water or on the treatment of waste water) towards an integrated, “ecosystem-based approach” protecting water ecosystems equally in terms of water quality, water quantity, ecological function and their role as habitats. However the requirements of the WFD are not easy to satisfy; approximately 50% of Europe’s water bodies will miss the WFD target and still be in poor ecological status in 2015 (EEA report 08/2012) although the situation is gradually improving.

The sixth Cohesion Report points out a variety regarding the performance in preserving aquatic ecosystems across the EU. *“In a number of regions, many water bodies have been subject to various kinds of action which have affected their hydrology (the movement, distribution and quality of water) or their morphology (through straightening water courses, canalisation or disrupting the connection to flood plains). This is particularly so for most regions in Belgium, the Netherlands, the Czech Republic, Germany, Poland and Hungary. In France, Sweden, Spain and the UK, water bodies in many regions have also been affected by such pressure.”*<sup>16</sup> Furthermore many of the changes would date back to the early industrial era, such as the straightening of the Rhine (which occurred between 1817 and 1876), or earlier, such as the reclamation of land from the sea in the Netherlands.

In general the reasons for challenges regarding water resources are manifold. Pressures on water resources, e.g. land use, water extraction, pollutions) are still strong while climate change is also affecting the natural cycle of water availability. These pressures are regionally variant. While Southern Europe is

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<sup>16</sup> European Commission, Investment for jobs and growth, Promoting development and good governance in EU regions and cities, Sixth report on economic, social and territorial cohesion, Brussels 2014, p. 124.

affected by droughts; Northern Europe is subject to other water hazards, e.g. floods.

At the same time the importance of water as an economic factor is an important driver in water related eco-innovation. Additionally the utility of hydropower is becoming more important, especially in the context of the Europe 2020 climate change mitigation targets, hence challenging the sensible balance of temporal, spatial and qualitative availability of water.

At the governance level the trend goes in to the direction of integrative management approaches, beyond administrative and national borders. This approach is evident in the establishment of regional or international management bodies, e.g. the ICPDR, the definition of River Basin Management Plan districts in the context of the WFD, the framework of the Integrate Coastal Zone Management indicated by the Marine Strategy Framework Directive etc.

#### *Perspective and role of the private sector*

The private sector is affected by the water policies and legislation of the EU and of the Member States in three aspects:

- Directly as a user of water for its business purposes, especially concerning pricing policy in accordance to WFD, Article 9, paragraph 1;
- Indirectly by the regulation of emissions and pressure on water bodies;
- And as a provider of services and solutions in the context of water management, utilities and water related eco-innovation.

#### *Role of the public sector*

The public sector is affected by the water policies and legislation of the EU and of the Member States in three aspects:

- At the national and regional level (depending on the type of governance) for the transposition, implementation, monitoring and enforcement of Union legal acts in the field;
- At the regional and local level for the construction and operation of public utilities networks, physical infrastructure and other related works for the use and protection of water resources (i.e. the traditional sectoral approach). The ESIF are an important factor in this field;
- At all levels for the integration of the new governance imperatives considering management approaches e.g. for the RBMP. The ESIF can usually offer the means for pioneer efforts.

### Role of the EU

Environment is a sector where the EU plays a central role in the definition of the strategic direction. The WFD provides the cornerstone for water protection and management in the European Community. Member States are obliged to introduce an integrated protection and management cycle ranging from analysis of the status quo by individual river basin and district, the definition of objectives, management plans and programmes of measures and the monitoring and reporting of progress in comparison to the original situation. An important companion to the WFD is the Floods Directive (2007/60/EC), which aims to foster flood risk management plans significantly enhancing the objectives of the WFD.

Earlier EU water policies are still relevant, e.g. the Urban Waste Water Directive (91/271/EEC), the Bathing Water Directive (2006/7/EC), the Nitrates Directive (91/676/EEC) and the Drinking Water Directive (98/83/EC).

### Perspective of LRAs

LRAs are assuming a responsive role in the water field, mainly as constructors and operators of public utility networks; in their traditional orientation they usually focus on compliance to the regulations and the satisfaction of the “given demand”.

The challenge and the perspective for LRA is the assumption of a management role for water resources, utilizing regulations, incentives and management and participation in the context of optimum satisfaction of the needs (rather than the “demand”) under the premise of minimization of pressure on water resources.

### **Waste**

Waste is a pressing environmental, social and economic issue. The wealth and growth of the western world and of Europe in particular was based on the intensive and industrial use of natural resources. In this process “waste” is generated at every stage, i.e. extraction, processing, production, distribution, consumption and final disposal and treatment. App. 5t of waste per capita was generated in 2008 in the EU. The largest waste “producers” are construction and demolition, mining and quarrying, and manufacturing; household waste is less than 10% of this figure. Hence waste generation was inseparable to growth.

### Major trends in a nutshell

Growth is needed to provide jobs and well-being to its citizens, at the same time is required to achieve a quality of this growth leads to a sustainable future.



Hence a fundamental transformation of the economy, decoupling growth from linear (or even exponential) resource consumption as well as a processing chain which excludes waste generation or engulfs recycling potential at every step are need. Preparing that transformation in a timely, predictable and controlled manner is crucial. Life-cycle approaches assess the process from “cradle to grave” and attribute impacts where they occur instead of concealing them by moving them to other countries or stages of production/consumption.

Also waste is not considered anymore as infinitely disposable but as a resource. This trend is driven by exhausting of disposal sites (or reaction towards their establishment) and scarcity of resources. Hence landfill of mixed solid waste is on the retreat, while recycling, composting and energy recovery use are becoming more popular. The differences between Member States however are substantial.

Finally the shift to a green economy renders recycling a significant source for technological, economic and social benefits through generating economic growth, innovation, employment and helping secure availability of critical resources.

#### *Perspective and role of the private sector*

The private sector is affected by the waste policies and legislation of the EU and of the Member States in three aspects:

- as a producer of waste concerning pricing policy in accordance to Directive 2008/98/EC on waste (Waste Framework Directive) and the polluter pay principle;
- as a contractor or partner of the public sector in the operation of waste management schemes;

And as a provider of services and solutions in the context of waste management, utilities and waste related eco-innovation.

#### *Role of the public sector*

The public sector is affected by the waste policies and legislation of the EU and of the Member States in two aspects:

- At the national and regional level (depending on the type of governance) for the transposition, implementation, monitoring and enforcement of Union legal acts in the field;

- At the regional and local level for the construction and operation of public utilities networks, physical infrastructure and other related works for the waste management, disposal and processing (i.e. the traditional sectoral approach). The ESIF are an important factor in this field.

### Role of the EU

EU legal instruments and strategies focus on waste prevention, i.e. decoupling waste generation from economic growth and environmental impacts according to the waste hierarchy principle (prevention before re-use, recycling and other recovery, disposal being the last resort). Examples are the revised Waste Framework Directive (WFD) (2008/98/EC) and the General Union Environment Action Programme to 2020 “Living well, within the limits of our planet”.

The former set recycling targets for special waste streams such as paper, metal, plastic and glass waste from households as well as for construction and demolition waste and obliged Member States to establish waste prevention programmes by the end of 2013 (Article 11.2 of the Directive).

Related issues are dealt with by the Landfill Directive (1999/31/EC), the Waste Incineration Directive (2000/76/EC), and the Industrial Emissions Directive (2010/75/EU).

### Perspective of LRAs

LRAs are assuming a responsive role in the waste field, mainly as constructors and operators of public utility networks; in their traditional orientation they usually focus on compliance to the regulations and the satisfaction of the “given demand”.

The challenge and the perspective for LRA is the assumption of a management and pro-active role for waste, utilizing regulations, incentives and management and participation in the context of optimum satisfaction of the needs (rather than the “demand”) under the premise of minimization of pressure on the natural environment.

A specific aspect of waste management facilities is that they are spatially bound; they consist so called Locally Unwanted Land Uses. Hence the role of the LRA is dual; a technical one regarding the selection of the best available technology and location and on the other one a mediating one related to the balance and interests of residents and neighbourhoods.

## Climate change

Tackling climate change is one of the great challenges facing the EU and its global partners. The IPCC defines climate change as “...any change in climate over time, whether due to natural variability or as a result of human activity.” The United Nations Framework Convention on Climate Change (UNFCCC) defines it as: ‘a change of climate which is attributed directly or indirectly to human activity that alters the composition of the global atmosphere and which is in addition to natural climate variability observed over comparable time periods.’ The sixth Cohesion Report highlights climate change as a world-wide process caused by human activities (greenhouse gases) and points at the facts that there are large variations in the potential impact of climate change on regions in Europe (in general a north-south divide). *“The general north-south divide in the effects which emerges, however, not only reflects the impact of climate change itself but also the greater capacity of Scandinavian and Western European countries to adapt to it. A medium-to-high impact can, therefore, be expected in large parts of South-East Europe as well as the Mediterranean regions.”*<sup>17</sup>

In the discussion on Climate Change it is distinguished between Mitigation i.e. the complex of efforts to reduce reducing total greenhouse gases (GHG) released in the atmosphere either by reducing emissions or by enhancing GHG capture and Adaptation i.e. the “adjustment in natural or human systems in response to actual or expected climatic stimuli or their effects, which moderates harm or exploits beneficial opportunities” according to the IPCC.

Mitigation and Adaptation are complementary strategies for reducing and managing the risks of climate change.

### Major trends in a nutshell

The IPCC Climate Change 2014 Synthesis Report claims that human influence on the climate system is clear, and recent anthropogenic emissions of GHG are the highest in history. Warming of the climate system is unequivocal; atmosphere and ocean have warmed, the amounts of snow and ice have diminished, and sea level has risen.

Regardless of causes, changes in climate such as extreme weather and climate events have caused impacts on natural and human systems, indicating the sensitivity of natural and human systems to changing climate. This trend amplifies existing risks and creates new risks of cyclical and cumulative nature for natural and human systems.

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<sup>17</sup> Sixth Cohesion Report, p. 100.

Globally causes and risks are unequally distributed; while GHG emissions are mainly stemming from the industrialized countries, risks are generally greater for disadvantaged people and communities in so called “developing” countries. For that reason the principle of shared responsibility is called upon. Decision making must be integrative and global and “informed by a wide range of analytical approaches for evaluating expected risks and benefits, recognizing the importance of governance, ethical dimensions, equity, value judgments, economic assessments and diverse perceptions and responses to risk and uncertainty” (IPCC, *ibid*).

An important trend in most European Countries is the formulation of National and Regional Risk Strategies and Adaptation Plans in accordance to international standards e.g. the ISO31010.

### *Perspective and role of the private sector*

The private sector is affected by the climate change policies and legislation of the EU and of the Member States in three aspects:

- On the Mitigation field, either as a subject to regulations (e.g. CO<sub>2</sub> taxes) or as a target group of incentives (related to the installation of renewable energy sources, the application of energy efficiency measures at the residential and professional field, the cultivation of biomass for CO<sub>2</sub> capture etc.) and as a carriers of behavioural and lifestyle choices.
- On the Adaptation field either directly as a subject to regulations (e.g. on hazard zones) and indirectly in the context of decision making, risk assessment and wealth valuation (e.g. related to business location decisions, property values etc.
- On both fields as provider of services, works and research results for the monitoring, forecasting of trends, the construction and operation of facilities and the provision of funding to the public sector.

### *Role of the public sector*

Through the international dimension of the climate change causes and impact, the need for integrative governance approaches is obvious. Many adaptation and mitigation options are available but no single option is sufficient by itself and in the short term. Effective implementation depends on the right mix of policies (e.g. regulation, technology development, diffusion and transfer, as well as finance) and cooperation at all levels (international, national, regional and local) and can be enhanced through integrated responses with other objectives.

Hence the role of the public sector can be seen in the following areas:

- In the field of Mitigation as a “trend-setter” in the demonstration of effective approaches, as financier of incentives programmes and finally as a regulator directly (e.g. by laws on emissions) or indirectly (e.g. by the promotion of mobility and settlement patterns that reduce the need for high energy consumption).
- In the field of Adaptation as a planning and management authority for land uses and risk zoning, as a provider of infrastructure and protective measures and in the support and regulation of risk insurance schemes.
- In both fields as a provider of scientific evidence and as a promoter of awareness.

### Role of the EU

In the field of Mitigation the Union has positioned itself clearly in the Europe 2020 Strategy and the 20/20/20 targets for climate change mitigation i.e. reduce GHG emissions by 20 % reduce energy consumption by 20 % through increased energy efficiency; and meet 20 % of energy needs from renewable sources. In this context the following must also be mentioned:

- Ratification of the Kyoto Protocol: this calls for 15 EU Member States (the 'EU-15') to reduce their collective emissions in the 2008 to 2012 period to 8 % below 1990 levels;
- Definition of the standards for energy efficiency of a wide array of equipment and household appliances;
- Definition of the framework for increased use of renewable energy sources, such as wind, solar, hydro and biomass, and of renewable transport fuels, such as bio-fuels;
- Development of carbon capture and storage (CCS) technologies;
- The establishment of the EU Emissions Trading System (EU ETS) and others.

In the field of Adaptation the EU has issued its “An EU Strategy on adaptation to climate change” in April 2013.

The ESIF have an important role to play in promoting climate action, especially in assisting Member States meet their mitigation commitments, co-financing the

necessary measures to enhance resilience and in meeting global demand for efficient and effective solutions. For that purpose at least 20 % of ESIF in the period 2014-2020 will contribute to climate change actions to strengthen energy security, promote a low-carbon, resource efficient and climate-resilient economy, enhance competitiveness and create more green jobs’.

### Perspective of LRAs

The integrative and overarching nature of climate change indicates the large scope of activities at the LRA level.

In the field of Mitigation the role of the LRA can be seen in the promotion and planning of low carbon zones by focusing spatially on energy savings, energy sufficiency and related interventions, as well as rich natural resources and renewable energies sources. LRA can also invest or support investment in the fields of technology development and innovation and reduce the dependency on imported fossil energy pursuing the status of low-carbon and energy sufficient model regions. However the achievement of such a status often fails not due to lack of suitable solutions but due to a weak “enabling environment”. This also concerns spatial development and growth debates, addressing a broad range of sectors related to energy inputs and emission outputs (from housing and buildings to agriculture and forestry), where LRA can and should act as a mediator.

In the field of Adaptation LRA assume primarily a regulatory role e.g. in planning and monitoring land uses and risk zoning and as a provider of infrastructure and protective measures (e.g. efficient water use, adapting building rules to future climate conditions and extreme weather events, building flood defenses and raising the levels of dykes). It also includes measures to take advantage of opportunities arising from climate change. The challenge and the perspective for LRA is also the assumption of a management role in dynamic climate change management, i.e. in adopting at the local level response and adaptation mechanisms that leave the path of conventional hazard abatement and focus on risk management. Such an approach puts however strains in the acceptance and awareness of the local population.

### **Nature and biodiversity**

A widely accepted definition of biodiversity is the one of the 1992 Convention on Biological Diversity, meaning “...the variability among living organisms from all sources including terrestrial, marine and other aquatic ecosystems and the ecological complexes of which they are a part; this includes diversity within species, between species and of ecosystems.”

Biodiversity is recognized as a cornerstone of healthy ecosystems, and biodiversity conservation is increasingly becoming one of the important aims of environmental management. Hence in this study the protection of biodiversity will be used as a surrogate of environmental protection in the broader sense.

### Major trends in a nutshell

As a global trend biodiversity is at the retreat, hence posing a risk to the provision of ecosystem services. The main causes are impacts in natural habitats and ecosystems due to intensive agriculture, urbanization and land abandonment production systems, construction, mining, forest diminishing, pollution of surface and ground water bodies, invasive alien species and global climate change.

At the political level the importance of biodiversity is gaining momentum; 2010 was the International Year for Biodiversity, where new biodiversity targets at European and global level. E.g. the EU has declared in the EU Biodiversity Strategy to 2020 that “By 2050 European Union biodiversity and the ecosystem services it provides – its natural capital – are protected, valued and appropriately restored for biodiversity's intrinsic value and for their essential contribution to human wellbeing and economic prosperity, and so that catastrophic changes caused by the loss of biodiversity are avoided” aiming at “Halting the loss of biodiversity and the degradation of ecosystem services in the EU by 2020, and restoring them in so far as feasible, while stepping up the EU contribution to averting global biodiversity loss”.

At the international level the Conference of the Parties (COP 12) held in 2014 strengthened the move from policy-making to implementation including the enhancement of cooperation and synergy within the three Rio Conventions and the biodiversity-related conventions.

A pivotal element in defining measures and policies for the protection of biodiversity is the establishment of reliable baselines upon which to measure success or failure. While elaborated indicators set are available, the reliability and interoperability of systems is still susceptible to debate; no single unified approach exists. Two tools for protecting biodiversity have been developed by the European Commission and EEA: the BISE and the ‘biodiversity baseline’. BISE, the Biodiversity Information System for Europe, both aiming to establish the evidence base necessary for planning actions.

Last but not least the importance of evaluating trade-offs and costs and benefits of biodiversity protection are becoming increasingly important in environmental management.

### Perspective and role of the private sector

The private sector is affected by the nature and biodiversity policies and legislation of the EU and of the Member States in three aspects:

- As an operating entity (private or business) affected by the degradation of ecosystems and the need to adapt to the loss of environmental public goods but also in developing innovative solutions to this problem.
- As a subject to regulations imposing restrictions on land use, activities etc.
- And as a citizen and taxpayer in the sense of her “willingness to pay” for the intrinsic non-use value of biodiversity.

### Role of the public sector

The public sector is affected by the nature and biodiversity policies and legislation of the EU and of the Member States in three aspects:

- At the national and regional level (depending on the type of governance) for the transposition, implementation, monitoring and enforcement of Union legal acts in the field;
- At the regional and local level for the planning and management of protected areas, in the monitoring of the status quo and at the local “on the ground” moderation and mediation among conflicting interests. The ESIF are an important factor in this field;
- At all levels for the integration of the new governance imperatives considering management approaches and the inclusion of the private and the voluntary sector. The ESIF can usually offer the means for pioneer efforts.

### Role of the EU

The role of the EU can be seen in three main areas, i.e.:

- In the field of policy formulation as defined in the EU Biodiversity Strategy to 2020, the EU's Forest Strategy etc.
- In the field of dynamic protection and risk management (protection, conservation and connectivity of “ecosystems”) e.g. as defined in the two mainstay pillars of the EU, namely the Directive 2009/147/EC 2009 on the conservation of wild birds (the Bird Directive) and the Directive 92/43/EEC (the Habitat Directive) along with the related Natura 2000



network but also Directive 2008/56/EC (Marine Strategy Framework Directive);

- In the field of sustainability and risk prevention with a number of Directives not directly related to biodiversity but limiting factors with an impact on it such as the WFD, Directive 91/676/EEC (Nitrate Directive), Directive 2008/1/EC concerning integrated pollution prevention and control (IPPC-Directive), Directive 2008/50/EC (Ambient Air Quality Directive), the CAP and the Common Fisheries Policy

### Perspective of LRAs

Environmental management and biodiversity protection has a very strong spatial aspect since on the one hand protective measures become manifest on single land plots and on the other hand in the sense that spatial planning and land use clearly influence biodiversity and thus ecosystem services.

The perspective for LRAs consists of:

- The management and response to the protection or loss of ecosystem services;
- The management of mainly habitats and ecosystem diversity e.g. through zoning and land use;
- The valorisation of a rich biodiversity as a locational advantage;
- The mobilization of the voluntary sector for the protection and monitoring of biodiversity;
- The exploitation of local strategies and bottom-up approaches for the accommodation of local interests under the regime of biodiversity protection.

### **Low-carbon economy and resource efficiency**

The Europe 2020 Strategy aims at sustainable growth by developing a more competitive low-carbon economy that makes efficient, sustainable use of resources. In the “Resource-efficient Europe” Flagship Initiative the aim is to “support the shift towards an economy that is efficient in the way it uses all resources, absolutely decouples economic growth from resource and energy use and its environmental impacts, reduces GHG emissions, enhances competitiveness through efficiency and innovation and promotes greater energy and resource security, including through reduced overall resource use”.

### Major trends in a nutshell

Worldwide, improved resource efficiency of production and consumption is a key requirement for sustainable growth; however resource extraction and consumption is constantly rising and accelerating. Global demographic and macroeconomic trends in Asia are expected to further accelerate this rate. This leads to high demand, market volatility and also to the strengthening of environmental problems, such as climate change, deforestation, loss of biodiversity and pollution. Technical solutions reducing the relative resource consumption tend to be ineffective in absolute numbers due to so called “rebound effects”.

Efforts towards a resource-efficient and low-carbon economy must fulfill three conditions:

- resource efficiency is a horizontal issue requiring coordinated action in a wide range of policy areas and needs political visibility, demonstration and support;
- initiatives are time-sensitive, and long investment lead- times require careful timing of interventions, even if some of them seem unattractive in the short term. The risks lie in the competition from globalised industry with low-price products and low environmental standards. This could lead to an industrial reluctance to accept legal changes towards resource efficiency that are perceived as too rigid;
- any change must be carried by the consumers, who must be encouraged to move to resource-efficient consumption, generate innovation and avoid rebound effects that can annihilate any specific efficiency gains.

### Perspective and role of the private sector

The private sector is directly influenced by the drive for resource efficiency due to the required complex approach and policy mix. These influences range from the availability and cost of raw resources for production, the energy supply options and costs, the use of “Best Available Techniques” e.g. in the context of the Industrial Emissions Directive, the requirement to apply monitoring and reporting procedures such as the LCA or ISO 14031 Environmental Performance Indicators, the application and development of eco-innovation, the need for financing and last but not least the changing preferences and tastes of the consumers. In this conglomerate the private sector is user, innovator and driver of resource efficiency.

### Role of the public sector

The main role of the public sector is related to the formulation of a framework that promotes resource efficiency. This can be done by:

- traditional “command and control” instruments such as regulations, legal acts etc.,
- market based approaches (environmentally related taxes, charges and subsidies, tradable permit systems, deposit-refund systems, environmental labelling, licenses, and economic property rights),
- promotion of partnership approaches (such as voluntary agreements, industry norms, eco-labels, participation at schemes such the UN GC or the GRI) and
- last but not least in the provision of long term stability for the development of resource efficient innovations and applications.

### Role of the EU

In general all aforementioned environmental policies favour resource efficiency. More explicitly two roadmaps are fundamental, namely the Energy Roadmap 2050 and the Roadmap to a Resource-efficient Europe. Briefly, they foresee the following indicative activities.

The Energy Roadmap:

- Considering energy demand: energy efficiency on new and existing buildings, new standards for consumer appliances, smart meters and transparency on energy consumption and pricing, provision of financing for consumers and businesses willing to invest in energy efficiency, and adapted urban and spatial planning.
- Considering the switch to renewable energy system sources (RES): market integration of RES, promotion of storage technologies, interconnection and smart grids, introduction of renewable heating and cooling.
- Considering the future of fossil fuels and alternative sources of energy: fostering the use of gas as an important link in the transformation of the energy system, promoting unconventional gas sources, introducing carbon capture and storage, considering the role of (imported) oil and (locally available) coal in the future energy mix, considering nuclear energy as a

decarbonisation option and developing alternative fuels, smart technologies and storage capacities.

- Considering the energy market: introducing new ways of managing electricity (i.e. market integration, penetration of RES and ability to recover investment costs, access to markets, capacity and flexibility of the energy regulators in the Member States), integrating local resources and centralised systems, especially in the light of RES, and renewal of the transmission and distribution networks. In this context, the request for a unified approach to attracting investors is mentioned, especially regarding carbon pricing, market imperfections, the need to support early movers and the role of public financial institutions such as the EIB and the EBRD.
- Lastly, the social dimension of the topic is underlined. For all these steps to be implemented public support is necessary and informing consumers is paramount. Simultaneously, support for vulnerable groups must be demonstrated.

#### The Roadmap to a Resource-efficient Europe:

- Setting up a framework for making and measuring progress: ensuring that stakeholders at all levels will be mobilised to ensure that policy, financing, investment, research and innovation are coherent and mutually reinforcing. In the context of creating a knowledge base, indicators should be defined to support public and private decision-makers, rendering resource efficiency a shared objective of the international community.
- Transforming the economy: e.g. improving products and affecting consumption patterns via price signals, environmental information and performance standards, boosting efficient production via policy incentives for efficiency investments.
- Turning waste into a resource: e.g. through separate collection systems and the establishment of functional markets for recycled raw materials, elimination of landfills and energy recovery of residuals.
- Supporting research and innovation: through substantial increases in investment, coherence in addressing the societal challenge of resource efficiency, climate change and resilience, and in gains from smart specialisation and cooperation within the European research area.
- Removing environmentally harmful subsidies: removing and abolishing environmentally harmful subsidies (EHS) and separating social or business support measures from subsidies that might hamper sound

environmental practice (e.g. artificially low electricity prices), shifting taxation from labour to resources consumption.

- Safeguarding ecosystem services: introducing an ecosystem services and natural capital valuation system, introducing an EU biodiversity strategy and assessment of the impact of agriculture and fisheries.
- Improving efficiency of natural resources and protecting air, land and water: ensuring security of supply, introducing a ‘circular economy’, where waste becomes a resource, taking lifecycle impacts into account, improving market structures and in the case of water ensuring the implementation of all Water Framework Directive (WFD) River Basin Management Plans. In the case of food, the inputs of the food production chain should be reduced by 20 percent.
- Improving the efficiency of buildings and transport: introducing the lifecycle approach, achieving nearly zero energy demand and minimising transport impacts on the environment.

### Perspective of LRAs

LRAs can have a saying in the following domains:

- In their own operating by adopting and promoting benchmarking and measurement methodologies such as Environmental Performance Indicators and Systems, LCA etc.;
- In creating a local market by applying green procurement criteria to public tenders;
- In providing locally adapted market incentives and training schemes;
- In promoting awareness of sustainable consumption and production patterns and changes in individual and societal behaviour and exploiting the benefits of local supply chains in terms of environmental protection, job creation and endogenous development.

### **Overarching and supporting systems**

Last but not least, environmental policy requires some additional “invisible” meta-elements to guarantee integration and to establish a coherent policy framework. The 7<sup>th</sup> EAP offers a good overview on what is to be achieved by 2020. These aims can be further aggregated in the following topics:

- Environmental compatibility ) addressing potential trade-offs in all policies in order to maximize synergies and avoid, reduce and, if possible, remedy unintended negative effects on the environment (e.g. through the Environmental Assessment Directive and other environmental and climate-related conditionalities and incentives in policy initiatives, including reviews and reforms of existing policy);
- Provision of evidence based through ex-ante assessments and ex-post evaluations and
- Closing data and knowledge gaps by using programmes such as Life and Horizon 2020 and tools and initiatives such as the Shared Environmental Information System SEIS, the European Pollutant Release and Transfer Register (PRTR), the EU ETS, the GMES/Galileo, the INSPIRE etc.

### **2.2.2 Labour market and social policies, health care**

High levels of unemployment, the introduction of atypical forms of employment and undeniable demographic changes have affected European labour markets and societies. With a growing risk of poverty and social unrest, the EU and national authorities recognized the need for short-term measures as well as structural changes in both, labour market and social policy.

The following paragraphs will illustrate the trends, challenges, responses and prospects faced in those policy fields.

#### **Major trends and challenges in a nutshell**

##### *Labour market*

Eurostat estimates that nearly 24 million men and women in the EU-28 were unemployed in March 2015 despite a slow recovery from the economic and financial crisis. Unemployment rates had increased dramatically in the crisis years particularly in a few countries, with youth and low-skilled workers being worse hit. As of February 2013, almost one out of four young people in the EU were unemployed; with rates as high as 58,4 and 55,7 percent in Greece and Spain, respectively.). Almost 30 per cent of youth in the EU were at risk of poverty or social exclusion in 2011. The European Commission's sixth Cohesion Report highlights the matter of fact that "*the crises, however, has wiped out half of the gains made*" in the period between 2000 and 2008.<sup>18</sup>

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<sup>18</sup> Sixth Cohesion Report, p. 57.

Since 2008, atypical forms of employment are on the rise, probably reflecting business uncertainty regarding demand prospects and the reluctance of employers to offer stable employment contracts given the prevailing uncertainty regarding future sales and production. In view of preventing layoffs in the crisis, more flexible working arrangements were concluded which led to the increase of temporary and part-time jobs.

### Social issues

As a result of the crisis, in 2012, 124,5 million people, or 24,8 percent of the populations, in the EU were at risk of poverty or social exclusion. A large proportion of these people are women and children. The rising levels of unemployment, the involuntary employment arrangements and the increase of poverty and social exclusion (particularly of young people) have led to social unrests in a number of EU countries.

Europeans are increasingly living longer (it is predicted that there will be a gain of five years in life expectancy by the year 2050), and families are having fewer children (average of 1,5 children per woman, i.e. below the 2,1 required to maintain population levels). The proportion of the population over the age of 65 in the EU-28 is expected to almost double in the next 40 years (17 percent in 2005; 30 percent by 2050). The proportion of the ‘very old’ – those over the age of 80 – is expected to more than triple by 2050. This demographic ageing will put pressure on public and private finances in two ways: retired workers will no longer be contributing tax revenue, and an older population will need substantially more in the way of care services (social care, health care), even if Europe’s older citizens on the whole enjoy better health.

At the same time, childcare provision can enable women to enter the workforce or keep in stable employment contracts.

Europe’s labour force has also been growing in recent years: Eurostat expects that at least 40 million people will have migrated to the EU by 2050. However, immigration only partially offsets the larger demographic trends. Immigration has increasingly become a hot topic, whether it concerns labour mobility within the EU or immigration from outside the EU, not just in terms of employment but also social integration.

### **Policy responses at EU level**

The ‘European semester’ created in 2010 runs from January to July every year and allows for a joint EU-level analysis of Member States’ economic policies and for the adoption of country-specific EU recommendations before governments draw up their draft budgets and submit them to national

parliamentary debate. A significant number of these recommendations address employment, social protection and inclusion (for example, labour market reforms, poverty, the inclusion of vulnerable people into the labour market, pension reforms, and so on).

The ‘open method of coordination’ (OMC) is a tool to ensure the policies implemented at national level are supported and complemented by the EU, although employment, social affairs and inclusion policies are put in place more effectively at Member State level.

### Labour market policy

One of the key targets contained in the Europe 2020 strategy is to have 75 percent of the active population (20–64 year-olds) in work by the end of the decade. In order to do so, the EU has taken various initiatives to support job creation (e.g. promoting social enterprises), restore the dynamics of labour markets (e.g. EU framework for anticipating economic restructuring) and improve EU governance (e.g. yearly bench marking and comparison of EU countries’ performance on the basis of selected employment indicators).

In particular, the EU is working to reduce the youth unemployment rate, which is more than twice as high as the rate for adults (23.6 percent in comparison to 9.5 percent in November 2013). The EU offers direct support to young people most in need, combined with structural reforms to enhance partnership, within all EU countries, between government departments, formal education systems, vocational education bodies, employment agencies, business, social partners and civil society organisations.

One example is the so-called Youth Guarantees, a package of measures for ‘moving youth into employment’ in April 2013. The Youth Guarantee is a comprehensive scheme which ensures that within 4 months of leaving formal education or becoming unemployed, young people up to the age of 25 receive a quality job offer, continued education, an apprenticeship or a traineeship. The European Alliance for Apprenticeships moreover brings together different public and private actors to improve the quantity, quality and image of apprenticeships.

### Social policy

One of the major targets of the Europe 2020 strategy is to lift at least 20 million people out of poverty by the end of the decade.

Although Member States themselves are responsible for organising and funding their own social protection systems, the EU plays a special role by coordinating



national social security systems, particularly with regard to mobility between EU countries.

In addition to the aforementioned policies and measures, social services have and will gain in importance given the economic, social and demographic changes. Better childcare provision can enable women to enter the workforce, while making it easier for families to have the number of children they want. Improved and more cost effective social care is also needed for Europe's older citizens.

In addition, immigrants must increasingly be seen as parts of European societies and therefore the policies and measures are to focus on the integration of migrants into the labour markets and societies. For instance, migrant workers have increasingly taken on jobs in the EU in care services which naturally responds to the market gap described above.

The European Commission defines social services as playing a crucial role in improving quality of life and providing social protection. They include:

- social security,
- employment and training services,
- social housing,
- child care,
- long-term care,
- social assistance services.

### **Key dimensions of labour market and social policy in relation to EU Cohesion Policy**

Labour market and social policies need to be considered as multi-faceted policies which should include a number of policy angles. The following table shows how the EU Cohesion Policy will support relevant measures in 2014-2020.

**Table 9. Support of labour market and social policy in the EU**

Labour market and social policy in EU Cohesion Policy	Description
Institutional and regulatory policy framework	<p>ESF, (ERDF):  ESF – Art. 3.1a),b)  ERDF - IP 8d)  ERDF - TO 9a),b),c)</p> <p>Based on the higher rates of unemployment, particularly for young people, the ESIF will focus more thoroughly on employment and (re-)integration measures in 2014-2020.</p> <p>Social protection and inclusion issues have also been put on the EU policy agenda even more prominently in the 2014-2020 programming period. Looking at the ESIF, particularly the ERDF has been focused more strongly on these policies, mainly with regards to social infrastructure, the increase of synergies with ESF actions, or strengthening the role of SMEs in social services. The same is true for the measures planned in the EAFRD (e.g. local social infrastructure such as childcare to encourage the employment of women; CLLD/ ITI initiatives).</p>
European Social Fund (ESF)	<p>Important role in supporting the EU policies and measures in the areas of employment and social policy. The role of the ESF has been reinforced for the 2014-2020 period. It is instrumental in helping EU countries respond to the EU's priorities and recommendations for national policy reforms in the fields of active labour market policies, social inclusion and employment policies, institutional capacity and public administration reform. 20 percent of each country's ESF allocation has to be spent on social inclusion projects and the Fund must account for at least 23.1 percent of the global cohesion policy funding at EU level, which will finally shape the total volume of ESF funding across the Member States.</p>

European Globalisation Fund (EGF)	<p>The EGF's role has been expanded to include workers made redundant because of an unexpected crisis, as well as categories of workers not previously covered by the EGF, for instance fixed-term and self-employed workers. In regions of high youth unemployment, the EGF can now fund measures for young people not in employment, education or training.</p> <p>The EGF has a maximum annual budget of EUR 150 million for the period 2014-2020. It can fund up to 60% of the cost of projects designed to help workers made redundant find another job or set up their own business. As a general rule, the EGF can be used only where over 500 workers are made redundant by a single company (including its suppliers and downstream producers), or if a large number of workers are laid off in a particular sector in one or more neighbouring regions.</p> <p>EGF cases are managed and implemented by national or regional authorities. Each project runs for 2 years.</p>
Fund for European Aid to the Most Deprived (FEAD)	<p>The FEAD has been allocated a maximum of €3.5 billion, in 2011 prices, for the 2014–20 period. This represents a slight increase in real terms, compared to the old food distribution programme. In addition, EU countries will provide 15 percent of national co-financing.</p>
EU programme for employment and social innovation (EaSI)	<p>The EaSI brings together the following three financial instruments managed by the European Commission in 2014-2020: European Progress Microfinance facility, Progress, European Network of Public Employment Services finance.</p> <p>As of January 2014, these programmes from the three axes of EaSI. They support:</p> <ul style="list-style-type: none"> <li>▪ the modernisation of employment and social policies with the PROGRESS axis (61 percent of the total budget);</li> <li>▪ job mobility with the EURES axis (18 percent of the total budget);</li> <li>▪ access to micro-finance and social entrepreneurship with the Microfinance and Social Entrepreneurship axis (21 percent of the total budget).</li> </ul> <p>The total budget for 2014-2020 is EUR 919,469,000 in 2013 prices.</p>

European Regional and Development Fund (ERDF)	<p>The ERDF aims to strengthen economic and social cohesion in the EU by correcting imbalances between its regions. In this light it supports regional and local development by co-financing investments in various policy measures, but also in employment and social infrastructures, particularly thanks the stronger focus on complementarity and synergies between funds in 2014-2020.</p> <p>The ERDF will also focus on productive investment, which contributes to creating and safeguarding sustainable jobs, through direct aid to investment in small and medium-sized enterprises (SMEs).</p>
European Agricultural and Rural Funds (EAFRD)	<p>The EAFRD is financed under Pillar II of the Common Agricultural Policy (CAP). It shall contribute to the Europe 2020 Strategy by promoting sustainable rural development throughout the Union in a complementary manner to the other instruments of the common agricultural policy (hereinafter "CAP"), to cohesion policy and to the common fisheries policy. It shall contribute to a more territorially and environmentally balanced, climate-friendly and resilient and innovative Union agricultural sector.</p> <p>In 2014-2020, the EAFRD will also focus on employment and social policy. In fact, one of the actions that will be supported is implementing schemes promoting the establishment of young farmers, but also actions aimed at promoting social inclusion, poverty reduction and economic development in rural areas.</p>
Youth Employment Initiative (YEI)	<p>With a budget of EUR 3 211.22 million (current prices) the YEI will reinforce the support already provided through the ESIF.</p> <p>YEI will target all young persons under the age of 25 not in employment, education or training, residing in eligible regions, who are inactive or unemployed including the long-term unemployed, and whether or not registered as seeking work. On a voluntary basis, Member States may decide to extend the target group to include young persons under the age of 30. For the purpose of the YEI for 2014-2015, "eligible regions" are those NUTS level 2 regions that have youth unemployment rates for young persons aged 15 to 24 of more than 25% in 2012 and for Member States where the youth unemployment rate has increased by more than 30% in 2012, NUTS level 2 regions that have youth unemployment rates of more than 20% in 2012.</p>

*Source: ESIF, EC official website, own considerations.*

### Perspective of LRAs

In addressing the societal challenges and financing constraints, national authorities are increasingly diversifying the ways in which these labour market and social policies are organised, provided and financed (e.g. increased decentralisation, outsourcing of certain tasks to private – profit or non-profit – providers). Consequently, a growing proportion of these services now come under the scope of Community rules on competition and the internal market employment, social affairs and inclusion policies are put in place more effectively at Member State level.

Good governance at national, regional and local levels is considered to be crucial and a stronger involvement of LRA has become a priority for the 2014-2020 programming period. The partnership principle was at the heart of the Cohesion policy reforms. Similarly, the 2014-2020 ESIF programmes offer more instruments to better involve relevant stakeholders in the implementation of the programmes: relevant ministries, regions, municipalities, professional organisations, research centres, businesses or social partners.

This is not least the case due to the focus on social problems and solutions not only in urban areas (e.g. local social infrastructure such as childcare to encourage the employment of women in urban as well as rural areas). In addition, the Community-led Local Development (CLLD) and ITI initiatives allow for an implementation of relevant measures at local level. CLLD is one of the ESF investment priorities under the TO9 and it targets local residents and beneficiaries as well as voluntary and community organisations, local authorities, other public authorities such as police, health and education, and local private sector businesses.

CLLD enables communities to use different funds to deliver projects that are responsive to the area's needs and to improve strategic local development. It presents opportunities to civil society organisations as our evidence demonstrates that the impact of CLLD is high on those groups furthest away from the labour market by increasing employment and skills, social enterprise, and social inclusion which leads to less poverty and better regeneration of deprived areas.

ITI will in turn implement territorial strategies in an integrated way. The actions to be implemented through ITI shall contribute to the thematic objectives of the relevant priority axes of the participating OP, as well as the development objectives of the territorial strategy. They can involve investments from the ERDF, ESF and CF. The funding can be complemented with support from the EAFRD or the EMFF.

It should be ensured that these instruments are used efficiently, since the involvement of a large number of different stakeholders, vertically and horizontally speaking, will be essential to reduce the unemployment rates in Europe (particularly concerning youth), social inequalities and effectively respond to economic and social challenges ahead.

### **2.2.3 Education and qualification**

Each EU country is responsible for its own education and training systems. The EU however plays a major role in supporting national action and help address common challenges, such as ageing societies, skills deficits in the workforce and global competition in terms of new and innovative sectors and jobs.

Education and qualification have increasingly gained in importance on the EU policy agenda and have been integrated across policy fields to ensure they play a key role in addressing the current challenges. Education is in fact, not least, a top priority in the Europe's 2020 strategy 'for smart, sustainable and inclusive growth'. Following the sixth Cohesion Report three benchmarks for 2020 have been set in addition to the headline targets for early-school leavers and participation in tertiary education (95 percent of children in early childhood education, less than 15 percent of 15-year olds with insufficient abilities in reading, mathematics and science and at least 15 percent of adults participating in lifelong learning).<sup>19</sup>

The following paragraphs will illustrate the trends, challenges, responses and prospects faced in relation to education and qualification.

#### **Major trends and challenges in a nutshell**

The economic crisis resulted in a dramatic rise in unemployment rates across Europe, with youth and low-skilled workers being worse hit. In 2013, almost every fourth young person was unemployed and in Greece and Spain, unemployment even hit every other young person.

However, according to the European Commission, unemployment is not merely caused by the crisis, but also by poor education and a lack of skills. About 20 percent of young people in the EU do not reach minimum levels of basic skills in reading, maths and science.

School leaving has also increasingly become a pressing issue in this context, with six million children leaving education and training with only lower secondary education or less. Considering that only one out of two adults with low skill levels is employed, whereas the employment rate for highly skilled

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<sup>19</sup> Sixth Cohesion Report, p. 66 (see also "EU policy responses" in this chapter).

adults is substantially higher, early school leaving is an important issue to be addressed in the next decade.

According to the European Commission, one of the main problems facing European job markets is the existing skills gap, i.e. a mismatch between the skills employers are looking for and those being offered by job-seekers.

Demand for skilled workers is likely to increase particularly in the most innovative and future-oriented sectors of the economy, such as engineering, science and technology.

Education and training are however also considered to be key tools for integrating marginalised groups such as migrants, the Roma and other minorities into the labour market and social life, but also reintegrating those who have been excluded due to economic circumstances and face difficulties in accessing jobs (e.g. older people, women).

In fact, migrants often face the problem that their skills and qualifications are not recognised. This again contributes to the above-described problems of the skills gap and unemployment.

### **Policy responses at EU level**

Each EU country is responsible for developing its own education, training and youth policies. Each national government can allow education matters to be treated at the regional or local level, as well as relevant institutions (e.g. universities).

The EU's role has therefore originally been to mainly ensure that Member States are aware and learn from each other's education, training, and youth policies. Students, apprentices, volunteers, teachers, youth workers, schools, universities and youth organisations can cooperate across borders. Consequently, the EU has developed cooperation programmes in education, training, and youth such as the Erasmus programme and Europe's first youth programme 'Youth for Europe'. With the signing of the Treaty of Maastricht (1993) formal European competences in the field of education, vocational training and youth were included in the Union's founding treaties.

The competencies have evolved in a way that the EU and its Member States now set the following benchmarks to be reached by 2020:

- The share of 15-year-olds with insufficient abilities in reading, maths and science should be smaller than 15 percent.
- School dropout rates from education and training aged 18-24 should be reduced to less than 10 percent.
- At least 40 percent of young adults aged 30 to 34 should complete higher education.
- At least 20 percent of higher education graduates and 6 percent of 18-34 year-olds with an initial vocational qualification should have spent a period of study or training abroad.
- At least 95 percent of children (from 4 to compulsory school age) should participate in early childhood education.
- At least 15 percent of adults should participate in lifelong learning.
- The share of employed graduates (aged 20-34 with at least upper secondary education attainment and having left education 1-3 years ago) should be at least 82 percent.<sup>20</sup>

Since 2010, with the approval of the Europe 2020 strategy, a variety of flagship initiatives have been launched, including:

- Youth on the Move (YotM): help better equip young people for the job market – which includes boosting the literacy of the less skilled – and to improve their education and training levels.
- The Agenda for new skills and jobs: literacy as an important part of the right mix of skills needed for success in the future labour market.
- The Digital Agenda for Europe: recognises the role of digital literacy for empowerment and participation in the digital era.
- The European Platform against Poverty and Social Exclusion: proposes the development of innovative education for deprived communities to help lift them out of poverty and social exclusion.

The EU is also focusing on improving the transparency and recognition of skills and qualifications to ensure that within and across borders, learners and workers

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<sup>20</sup> Sixth Cohesion Report, p. 66.



see their skills and qualifications quickly and easily recognised, which is essential to raise skill levels and increase employability.

Investing in education, skills and life-long learning through different EU funding programmes in fact also aims to contribute to increasing and improving social integration. Life-long learning (LLL) is key in this respect, as more has to be done to ensure that the skills of workers are increased and adapted to the current and future needs of the labour market throughout life, regardless of age.

### **Key dimensions of education and qualification in relation to EU Cohesion Policy**

Education and qualification policies need to be considered individually as well as cross-cutting policies integrated horizontally across policies. The following table shows how the EU Cohesion Policy will support relevant measures in 2014-2020.

*Table 10. Support of education and qualification in EU Cohesion Policy*

<b>Education and qualification in EU Cohesion Policy</b>	<b>Description</b>
Institutional and regulatory policy framework	<b>ESF, (ERDF):</b> ERDF - TO 10 ESF – Art. 3.1c)
European Social Fund (ESF)	Important role in supporting the EU policies and measures in the areas of education and qualification. The role of the ESF has been reinforced for the 2014-2020 period. 20 % of each country's ESF allocation has to be spent on social inclusion projects and the Fund must account for at least 23.1 percent of the global cohesion policy funding at EU level, which will finally shape the total volume of ESF funding across the Member States. In terms of education, the ESF aims at boosting the adaptability of workers with new skills, and enterprises with new ways of working.
European Regional and Development Fund (ERDF)	The ERDF aims to strengthen economic and social cohesion in the EU by correcting imbalances between its regions. In this light it supports regional and local development by co-financing investments in various policy measures, but also in education and social infrastructures, particularly thanks the stronger focus on complementarity and synergies between funds in 2014-2020.

European Agricultural and Rural Funds (EAFRD)	<p>The EAFRD is financed under Pillar II of the Common Agricultural Policy (CAP). It shall contribute to the Europe 2020 Strategy by promoting sustainable rural development throughout the Union in a complementary manner to the other instruments of the common agricultural policy (hereinafter “CAP”), to cohesion policy and to the common fisheries policy. It shall contribute to a more territorially and environmentally balanced, climate-friendly and resilient and innovative Union agricultural sector.</p> <p>In 2014-2020, the EAFRD will also focus on education. In fact, one of the actions that will be supported is vocational training to ultimately increase competitiveness.</p>
Youth Employment Initiative (YEI)	<p>With a budget of EUR 3 211.22 million (current prices) the YEI will reinforce the support already provided through the ESIF.</p> <p>YEI will target all young persons under the age of 25 not in employment, education or training, residing in eligible regions, who are inactive or unemployed including the long-term unemployed, and whether or not registered as seeking work. On a voluntary basis, Member States may decide to extend the target group to include young persons under the age of 30.</p> <p>For the purpose of the YEI for 2014-2015, "eligible regions" are those NUTS level 2 regions that have youth unemployment rates for young persons aged 15 to 24 of more than 25% in 2012 and for Member States where the youth unemployment rate has increased by more than 30% in 2012, NUTS level 2 regions that have youth unemployment rates of more than 20% in 2012.</p>

*Source: ESIF, EC official website, own considerations.*

### Perspective of LRAs

The partnership principle characterised the shape Cohesion policy has taken for the 2014-2020 period. Multi-level governance has ensured that a large number of different types of actors have and will be involved in developing and implementing the ESIF programmes.

Particularly given the cross-policy relevance of education, it is important that LRA and social partners work together on the implementation of education measures at all levels of administration.

The activities that should particularly be supported at regional and local level are: educational and social infrastructure, LLL and measures aiming at adapting the skills to the current and future needs on the labour market, education measures for migrants, education measures for women and older people who have been excluded from the labour market, initiatives aiming at reducing drop-out levels, activities which aim to exchange knowledge and experience in those fields.

The Community-led Local Development (CLLD) and Integrated Territorial Investment (ITI) initiatives allow for an implementation of relevant measures at local level.

By allowing the use of different funds in the projects implemented at local level, the CLLD initiative responds to the areas' needs and improves strategic local development. It can thereby have an impact on the (re-)integration of groups further away from the labour market by increasing employment and skills. The same is true for activities supported through ITIs.

These instruments should ultimately help improving the access to education for all socially and economically excluded groups to reduce the unemployment rates in Europe (particularly concerning youth), social inequalities and effectively respond to economic and social challenges ahead.

## **2.2.4 Research and innovation**

RDTI or also STI (Science, Technology and Innovation) is perceived as the key factor in productivity growth and thus the key driver for competitiveness in a global economy. The most remarkable challenges in this policy field stem from the internationalisation and globalisation in the economy with immediate repercussions on this policy field: there is a pressing need to reform national policy approaches in favour of more open governance models. National approaches also have to acknowledge that technological development is but one element of innovation – nowadays the most innovative companies combine several modes of innovation (e.g. technological development paired with marketing and organisational development).

### **Major trends in a nutshell**

#### *Global Value Chains replacing the notion of high-value productions*

The past two decades have been marked by an increasing dispersion of business activities. The second layer in competition next to market shares in high-value industries is now the competition for high value activities in Global Value Chains (GVCs) – this has added a new dimension in STI policies which is

largely beyond the scope of national innovation policies.<sup>21</sup> Innovation enables economies to reach higher segments in global value chains. The highest value is often in upstream (e.g. new concept, manufacturing of key components) or downstream (e.g. in marketing, branding and consumer service).

### Accelerated knowledge flows between interconnected knowledge hubs

In parallel STI has seen the emergence of globally interconnected knowledge hubs. Asia is on the rise in global R&D. The world investment in R&D has increased steadily since 2007<sup>22</sup> whereas in contrast the share of global R&D investment in USA (28 percent in 2012), Japan (10 percent) and EU (20 percent) has decreased steadily. At a global scale China is on the rise, the world leaders in R&D intensity are Korea and Israel. The leaders in EU in Gross R&D expenditure as percent of GDP are FI, SE, DK, DE (their role as innovation leaders largely owed to the fact that key STI units of numerous MNEs have the seat in these countries and apparently work in close cooperation with the public sector). In case that the national economy lacks innovation leaders it is becoming increasingly difficult for smaller countries to reach world-class level thus bearing the risk to be excluded from GVCs and global knowledge flows. A major point is also that production of knowledge is increasingly decoupled from its use which clearly shows limits to comparatively narrow cluster approaches built on a small notion of product or process innovation.

A further trend – fuelled by internationalisation – is the acceleration in technological development combined with a high concentration in relatively few sectors (pharmaceutics and biotechnology, technology hardware, automotive industries account for half of the global R&D investment). Other sectors have experienced recent bursts in patent filing which mark breakthroughs in development such as e.g. in:

- climate change mitigation (lighting, power etc.),
- ageing, health and food,
- information and communication management,
- new manufacturing processes (chemistry, nanotechnology, laser, 3D printing etc.).

### Perspective and role of the private sector

From the perspective of companies decisions on innovation depend mainly on:<sup>23</sup>

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<sup>21</sup> Cf. OECD 2014, p. 236.

<sup>22</sup> Cf. OECD 2014, p. 54.

<sup>23</sup> Cf. OECD 2014, p. 22.

- The firms anticipation of future innovation.
- The profitability of the current business activities (based on previous innovations).
- The market prospects and favourable macroeconomic conditions.
- The protection of Intellectual Property Rights has become increasingly important.

In general firms are drivers in innovation but tend to under invest in R&D (due to costs, uncertainty of success, time required etc.) – the size of companies plays a decisive role: large multinational companies are key actors in business R&D. Albeit there is a clear impact of the crisis: companies become more risk averse and concentrate on innovations with short-term benefits.<sup>24</sup> With the need for fiscal consolidation in many MS the growing tax burden increasingly discourages private R&D investment.

Size and growth of markets have been traditionally the most important factors for the location of Foreign Direct Investment (FDI) – the past decade has seen a growing role of strategic assets such as knowledge, presence of suppliers, competitors and lead users. In short major assets in terms of STI are becoming increasingly important for national and regional success in FDI.

### **Role of the public sector and the EU**

In most MS usually several ministries are in charge of economic competitiveness, innovation and skills development and with the growing need for efficiency and effectiveness there is an inherent tendency towards an ‘whole-of-government approach.’ In previous periods public RDTI has often been used counter-cyclical and reinforced during times of economic downturn; the presumed unsustainability of public debt and the lingering crisis have put an end to this role. One visible sign in OECD countries is the cutback on public spending for energy and environmental issues since 2009.

The EU has persistently strengthened its position and role in STI. The EU seeks to establish European STI governance which is striving for complementarities and gains in effectiveness and efficiency and the pooling of financial resources, thereby trying to overcome the limits of national policy patterns such as concerns about distribution of benefits.

EU 2020 marks a switch from hard investment (physical infrastructure) to soft factors in particular skills and STI. Four out of seven flagship initiatives have a more or less direct link to STI policies:

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<sup>24</sup> OECD 2014, p. 68.

- Innovation Union – targeting financial resources for STI.
- Resource-efficient Europe: energy efficiency, renewable energy, reduction of carbon emissions – these developments depend to a large extent on dedicated STI policies with as strong public component.
- An Industrial Policy for the Globalisation Era – the development of a competitive and sustainable industrial base in Europe depends to a significant extent on a successful and enabling STI environment.
- Digital Agenda for Europe – ICT is generally perceived as key enabling technology for STI.

Smart specialisation Strategies (also referred to as S3) have become the strategic anchor point in EU policies on RDTI (STI). One of the major points of departure for this approach has been the argument that the effectiveness and efficiency of research investment in the EU was hampered by fragmentation, lack of coordination and insufficient critical mass – at the same time investments tended towards a quite narrow range of areas such as ICTs, nano- and biotechnologies.<sup>25</sup> Smart specialisation strives for a bottom-up or shared learning process resting on entrepreneurial discovery of prospective areas for future specialisation. Major new elements in the process are:

- the focus market growth potential and innovation needs,
- replacing the previous focus on internal linkages with an outward-looking perspective, i.e. a focus on comparative advantages in a European and global context.

In practice it should lead to cross-sectorial orientation on value chain development and corresponding targeted support for essential R&D activities but also encompassing up- and downstream activities.

The major sources of support at European level in the period 2014-2020 are:

- Horizon 2020 (also H2020) the European STI programme foresees about 80 billion EUR which are granted based on competitive calls mainly to companies – compared to its predecessor there is a shift to near to market R&D and a greater emphasis upon social challenges; many underlying tools supporting the implementation process e.g. initiatives born under the European Research Area (ERA) such as ERA-nets, Joint Technology Initiatives etc.

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<sup>25</sup> See also JRC 2014a).

- The ESIF with a foreseeable investment volume of about 100 billion EUR. for innovation which – despite its entirely different mechanism for allocation of funds can have decisive role to raise the leverage of H2020 mainly through: *funding of upstream projects (i.e. the building of knowledge generating capabilities that in the future can become eligible for H2020 funding) and also downstream projects (i.e. more direct innovation supporting activities that support innovation outcomes from H2020 projects and other activities*<sup>26</sup>.

In terms of policy instruments an increasing focus of STI policies on restoring productivity growth has to be stated. The following table shows major tendencies in policy instruments which have currently become visible in OECD countries and links these to the options in Cohesion Policy.<sup>27</sup>

**Table 11. Trends in STI policy instruments and relevance of EU Cohesion Policy**

<b>Instruments / policy approach</b>	<b>Relevance of EU Cohesion Policy and other European policies as driver</b>
<b><i>STI infrastructure</i></b>	
<u>Research excellence</u> Structuring public research around centres of excellence – fostering quality and relevance of scientific production while containing costs; the policies aim at a faster knowledge spill over to the economy – public institutes experience a shift from institutional core funding (block grants) to project funding; new policies oscillate between stable funds and competitive elements – many countries have established research excellence initiatives (e.g. in DE)	Reflected in Thematic Objectives (TO) 1) and 4) of ERDF but also an implicit focus of Horizon 2020
<b><i>Capacity building for STI</i></b>	
<u>Internationalisation in STI</u> Fostering capacity of firms and institutions to integrate international knowledge flows (international RDTI investments, mobility of researchers and students, cross-border governance of S&T) - e.g. DE (mobility programmes) or UK (international education council) have launched national strategies for the internationalisation of their higher education or DK (Tope Talent Denmark – oriented towards talents from Asia)	Key objective of Horizon 2020 (H2020)
<u>Building entrepreneurship in STI</u> Fostering entrepreneurship (training, management and incubators, agencies at universities) and facilitating funding (venture and risk capital, tax incentives)	ERDFTO 1, option to develop financial instruments ESF – Art. 3.2a),b)

<sup>26</sup> JRC 2014a), p. 9.

<sup>27</sup> OECD 2014, p. 36.

<b><i>Governance approaches to STI</i></b>	
<u>Funding leverage</u> Public Private Partnerships (PPPs) in STI with the rationale of improving the leverage of public support to business R&D and share risks; PPPs bear increasing opportunities for commercial spillovers from public research and might range from small-scale temporary projects to longer-term joint ventures (subject of PPPs are now often soft infrastructures such as databases or software; public initiative is launched with specific Calls (ES), or programmes (such as the programme on centres for competence in CZ); but one has to note practical difficulties for cross-border PPPs due to differences in legal frameworks	Inherent objective of H2020
<u>Public Procurement as instrument</u> Trend towards greater use of public procurement as demand-side instrument to stimulate RDTI – e.g. DE (German procurement law and centre of excellence for innovative procurement)	National reform task; supported due to the comparatively new options in the EU Procurement Directive
<u>Greening the economy</u> For Europe with its scarce raw materials and high population density greening the economy or the Green Agenda is a major cross-cutting policy topic– STI is essential to further this agenda. The Green Agenda requires public investment in fundamental (basic) and long-term research. STI in MS reveals currently a focus on energy related R&D.	Cross-cutting objective of Cohesion Policy based on thematic concentration and requirements to contribute to climate change mitigation; also key objective of H2020
<u>Focussing STI support</u> Streamlining and concentrating innovation support	National reform task; eventually fostered by ex-ante conditionalities

*Source: OECD 2014, own considerations.*

Speaking of traditional instruments in national public RDTI support – i.e. in particular direct support and tax incentives – the recent past has seen a rise of R&D tax arrangements since options for direct state aid have been capped and the available public funds have stagnated.<sup>28</sup> Another trend was that in general the groups of potential beneficiaries have been broadened for all support instruments. In the EU the most usual approach is a combination of direct (grants, loans) and indirect incentives (tax arrangements): the MS HU and FR have set-up the most generous offers. A general criticism is that tax incentives rather encourage short-term applied R&D and paired with profit-shifting strategies of many Multi-national Enterprises (MNE). The erosion of the tax base has increasingly come into the public debate. Some MS offer no fiscal R&D incentives, e.g. FI, DE, SE – these are the MS where gross public expenditure for RDTI is the highest.

<sup>28</sup> Cf. OECD 2014, pp. 68- 69.



Most MS have embedded their national strategies on STI in EU 2020<sup>29</sup>. The strategy focus is on emerging and enabling technologies (cognitive sciences, nanotechnology, and biotechnology) and the establishment of flexible and versatile catalyst institutions such as convergence hubs and technological platforms. The trend in MS policies points towards interdisciplinary approaches, cooperative projects, and an encouragement for technology monitoring and foresight analysis.<sup>30</sup> Generally speaking in STI the underlying process of strategy development is more important than the strategy document itself since the process is the key opportunity to raise interest, to identify barriers and to strengthen cooperation and commitment of the actors involved.

## **Perspectives for LRAs**

### *STI policies require corporate governance*

In general a leading role in STI is difficult to be reached and kept from a national perspective. In particular for small MS the opportunities for success with stand-alone approaches in STI are limited. This applies the more so when it comes to the level of LRAs: modern and successful STI policies require a broad approach with marked features of MLG. In the end LRAs can be targets of national policy efforts or places where unintended impacts are felt.<sup>31</sup>

Key elements for virtuous circles in STI have to be considered as a pre-dominantly national agenda, i.e. the national level has a lead function and the scope of action for LRAs is strongly dependent on the national efforts. Examples of such key elements of national STI policies are:

- strengthening the quality and absorptive capacity of the domestic science base,
- excellence initiatives in R&D and building knowledge hubs,
- the strategic focus of wider policy areas with significant impact on STI such as tax or immigration laws.

For obvious reasons the actual weight of LRAs in STI policies depends to a significant extent on the institutional and territorial architecture of the MS. In federal MS such as DE, AT or IT regions play a visible role in STI policies – regions do run their own support programmes, do have their own intermediaries such as agencies building capacities and fostering the implementation of Regional Innovation Strategies (RIS) and have become increasingly managers and owners of higher education infrastructure as well as of technology centers and science parks. Since success in the current approach of regional Innovation

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<sup>29</sup> Cf. OECD 2014, p. 92.

<sup>30</sup> Cf. OECD 2014, p. 62.

<sup>31</sup> Cf. also JRC 2014.

and Smart Specialisation Strategies (RIS3) requires strong policy coordination it offers in principle new opportunities for LRAs but the approach has to be open to external views and for the inclusion of the private sector. Thus in the end its success depends on new approaches to governance and management of public resources for STI. The policy debate on RIS3 emphasises the need to rethink previous approaches:

*“The essence of the entrepreneurial discovery process lies in its interactive nature that brings the different actors together in a participatory leadership process to carve out jointly the smart specialisation fields and develop a suitable policy mix to implement it [...] This means that the regional government no longer plays a role of omniscient planner but it will assess the potential of the new activities and empower those actors which are most capable of realizing that potential.”<sup>32</sup>*

An important element in the RIS and RIS3 process is also the cooperation among regions – an approach which is encouraged by the macro-regional strategies of the EU and the ETC programmes as policy lever for regional cooperation in STI.

#### STI policies as a particular challenge in rural areas

The sixth Cohesion Report underlines the challenging situation for rural areas to some extent: *“R&D expenditure is generally high in regions with a large city, though the regions with the largest city, which is usually the capital, do not in all cases have the highest levels. Indeed, many regions with high expenditure do not have a very large city, such as Oulu in Finland or Styria in Austria. In part, this is because very large cities tend to have a smaller share of activity in manufacturing, which generates most R&D.”* However, the report also says that R&D by no means captures all expenditure on innovation.<sup>33</sup>

The image of innovative regions is still shaped by clustering in knowledge-driven sectors and the vital knowledge spill-overs to small and new firms which in turn refuel innovatory processes. The focus on STI has an inherent and understandable tendency towards urban areas as engines of growth offering the essential milieu for innovation. E.g. a study combining economic modelling and interviews came to the following conclusion: *The findings also imply that ‘soft’ instruments are most effective in technologically more advanced regions where sufficient agglomeration of knowledge activities is found alongside dense interregional research collaboration linkages, high levels of social capital and good physical accessibility.*<sup>34</sup>

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<sup>32</sup> CF the website of the JRC on S3 (<http://s3platform.jrc.ec.europa.eu/>).

<sup>33</sup> Sixth Cohesion Report, p. 29.

<sup>34</sup> CF LSE 2011, p. 14.

Literature suggests that the challenge for LRAs in rural areas is even greater to trigger processes of innovatory development. First of all *innovatory economic development [in rural areas] is more likely to be understood in terms of social innovation (to encourage local linkage and collective learning cultures) and cultural innovation (to improve the rural milieu).*

Next to overcoming the traditional notion of innovation as industrial innovation the key element for approaches to S3 in rural areas is the outward looking perspective, the combination of local and external knowledge in order to foster diversification. Recent research of JRC has identified three key elements<sup>35</sup> for successful innovation approaches in rural areas– noteworthy is the dominance of policy-related factors:

- Identification of promising niche products.
- Resources and conditions required to develop an effective policy.
- To overcome policy-path dependency and to reach the *institutional sustainability threshold*.

### **2.2.5 Network development and infrastructure**

The EU has one of the densest transport networks in the world reflecting its population density and resulting transport demand. Transport demand is especially high in urban, industrial and other densely populated areas.

Trans-European Networks (TEN) exist in three infrastructure sectors; transport; energy and telecommunications. In Short TEN are the European dimension of these key networks promoting the interconnection and interoperability of the national networks as well as the access to such networks. Art. 170 of the Treaty on the Functioning of the European Union provides the legal basis for Trans-European Networks (TEN), Article 170 refers explicitly to the linking of peripheral, island or landlocked regions to the TEN. Three EU regulations deal with three TEN infrastructure sectors separately.

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<sup>35</sup> Cf. JRC 2014, p. 16.

**Table 12. TEN and CEF 2014-2020**

<i>Sector</i>	<i>TEN network length</i>	<i>Investment required until 2020</i>	<i>CEF contribution</i>
Transport	Comprehensive network: - 138,072 km of railway lines - 136,706 km of roads - 23,506 km of inland waterways  Thereof core network - 68,915 km of railway lines - 59,630 km of roads - 23,506 km of inland waterways	500 BEUR Thereof 250 BEUR for the core network	26.25 BEUR (thereof 11.3 BEUR from CF)
Energy	n.a.	200 BEUR for electricity and gas infrastructure of EU relevance 1,000 BEUR total investment need in EU energy infrastructure	5.85 BEUR
Telecommunications	n.a.	n.a.	1.14 BEUR
Total TEN	-	970 BEUR	33.24 BEUR

Sources: CEF Regulation, Preamble, DG MOVE<sup>36</sup>.

In addition to grants, innovative financing instruments developed in cooperation with financing institutions like the European Investment Bank are used (Marguerite Funds, Loan Guarantee for TEN Transport LGTT, Project Bond Initiative).

The budget breakdown already hints at the substantial role of transport. Whereas in the energy and telecommunications sectors, public financing is considered as a complementary source to private financing in case of market failure and the role of the public is more in regulatory policies, the provision – i.e. planning and funding - of transport infrastructure is traditionally seen as a task of the public sector.

The three infrastructure networks play a decisive role in reaching the Europe 2020 targets given their fundamental role for all economic activities. In all three sectors, there is the challenge of securing private investment and open competition with its efficiency advantages in markets that can to some extent be

<sup>36</sup> Please see: [http://ec.europa.eu/transport/themes/infrastructure/ten-t-guidelines/maps\\_en.htm](http://ec.europa.eu/transport/themes/infrastructure/ten-t-guidelines/maps_en.htm).

considered as natural monopolies. EU policy fosters models of separation of loss-making and thus usually publicly owned and financed infrastructure from operations where a common open market is envisaged. However, across all three sectors leverage of private funding is also an issue for infrastructure investment albeit so far with limited success (in particular in transport<sup>37</sup>).

*Key challenge: mobilisation and coordination of investment*

The facts and figures provided above point clearly at the overarching challenge linked to the TEN initiative: it is the mobilisation of – primarily public – investment and coordination of the implementation across the MS.

When comparing the direct EU-funding made available until 2020 and the estimated investment need – in particular in the field of transport – the enormous funding gap is apparent. Given the current budgetary constraints throughout the EU a realisation of the network according to plan does not seem realistic.

## **Transport**

The trans-European transport network (TEN-T) is a network which comprises roads, railway lines, inland waterways, inland and maritime ports, airports and rail-road terminals throughout the 28 Member States. The TEN-T consists of two planning layers:

- The "comprehensive network": a multi-modal network of relatively high density, the planning of which has been based on a number of common criteria (e.g. volume thresholds for terminals or accessibility needs).
- The "core network": a part of the comprehensive network, distinguished by its strategic importance for major European and global transport flows, resulting from a European planning methodology developed by the European Commission and subjected to broad consultation among Member States and other stakeholders.

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<sup>37</sup> With notable exceptions of the (only partially successful) PPP models in motorway construction and the relatively common PPP structures in port and dry port development. Cf. Roumboutsos et. al. 2014.

### TEN-T network size:<sup>38</sup>

**Table 13. TEN-T Network**<sup>39</sup>

Transport mode	Network in km - 2003	Network in km - 2020
Rail	83,300	:
Road	74,500	95,700
Inland waterways	14,100	:

Source: DG Energy and Transport, Eurostat.

The intended investment volume shows vast difference between MS with major focus in IT and ES (about 70 bn EUR each, FR 43 - PT, UK, DE, GR 20 - AT 17). The table illustrates that main network expansion is concentrated on road as the most important transport mode (see below), whereas investment in rail rather focuses on upgrading existing lines and major expansion projects of the inland waterway network are not planned in the medium term.

## **Major trends in a nutshell**

### Trends in traffic flows

In passenger transport, the passenger car remains by far the most important mode of transport (almost three quarters of passenger-km in with a stable modal share over the past 20 years). The fastest growing mode since 1995 has been aerial transport (+65 percent), tram and metro show moderate growth, the rail share remains stable (6.5 percent) whereas bus and water transport have lost market shares.<sup>40</sup>

High speed rail products have come under heavy pressure on the market by low-cost air carriers and long-distance bus transports. On the other hand side, urban rail is profiting from the increasing problems of road transport in cities (congestion, lack of parking space resulting in tolls and parking restrictions).

As for freight transport, the most important transport mode and the only one with growing modal share is road (almost three quarters of inland transport). Sea transport has remained stable over the past 20 years, whereas the other inland transport modes, rail (17 % in 2012), inland waterways (6 percent in 2012) and pipelines, are losing market shares<sup>41</sup>.

A major trend in the freight transport sector is increasing containerisation of goods and multimodality of transport chains. This opens up new opportunities for rail and inland waterways transport, two transport modes that have been

<sup>38</sup> Website DG Move: <http://ec.europa.eu/transport/infrastructure/tentec/tentec-portal/site/en/keyfacts.html>

<sup>39</sup> Date differ from the data given above that depict the status quo of 2014 with a changed TEN network.

<sup>40</sup> EU Transport in Figures – Statistical Pocketbook 2014.

<sup>41</sup> EU Transport in Figures – Statistical Pocketbook 2014.

disadvantaged by the change in the industrial structure of Europe in the past decades gradually losing their traditional business of transporting heavy industry goods. Container block trains with the last mile carried out by road have become the most important growth market in the rail sector.

New logistics concepts like just-in-time or just-in-sequence, shrinking size of individual consignments, the rise of courier, express and parcel services as well as sinking transport rates exert constant pressure on logistics improvement and productivity increase. These developments clearly favour transport modes with inherent flexibility that are dominated by private operators, road and air.

### Infrastructure development

In road transport for the past decade in Cohesion Policy the expansion of the motorway network has accounted for significant investment volumes. Motorway construction has been widely regarded as essential for the economic catch-up process: the process has been particularly marked in the MS ES<sup>42</sup> but e.g. in relative terms also in IE; upon the accession wave in 2004 the completion, construction of the network has been in the focus of CF investment in EU12(13).<sup>43</sup>

Generally speaking the focus in rail transport has been less on network expansion but increasing speed and capacities. One indicator of pending investment needs are the marked gradients as regards the electrification of the network within the EU.<sup>44</sup> In rail transport the most significant investment volume has been targeted towards the development and expansion of the high-speed rail network (about 9,600 km until about 2003; e.g. in DE, FR, ES) and the upgrading of passenger railway stations and intermodal freight terminals.

In inland waterways the NL are by far the MS with the highest density. Regions with significant stretches can also be found in DE and FR. In terms of investment the upgrade of ports (in terms of strengthening their role as multimodal hubs) is clearly in the centre. Plans for network expansion are there but tend to be rated as large-scale investments with low probability of implementation.

As regards air transport investment in airports co-funded from SF has been a frequent phenomenon across the Cohesion countries in the EU. For the period 2014-2020 the role of ESIF has been restricted to investment in favour of

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<sup>42</sup> Cf. Eurostat website: inland transport Infrastructure at regional level – five out of the ten regions with the longest motorway stretches constructed in the period 2000-12 are in Spain (accounting for a total of 1,765 km!)

<sup>43</sup> E.g. development of the trunk network in PL, construction of ring motorways around the capitals of HU and SK etc.

<sup>44</sup> Cf. Eurostat website: e.g. LU 95%, BE 86%, SE and NL 75% in comparison to GR, LV, LT, EE with shares of about 20%.

environmental protection.<sup>45</sup> Next to environmental concerns this is also owed to the fact that airports are usually profit-oriented and thus fall under state aid regulations.<sup>46</sup>

Regarding seaports, investment concentrates on the introduction and upgrade of container ports and terminals in order to keep pace with increasing container handling volumes and the size increase in container ships (up to 19,000 TEU at the moment; i.e. almost 10,000 sea containers) as well as changes in energy trade patterns requiring additional facilities for gas storage<sup>47</sup>.

### Challenges inherent to developments in the transport sector

There is the environmental challenge. Transport accounts for 31.8 percent of final energy consumption in the European Union, more than any other sector - while employing 5 percent of total EU workforce and contributing 4.8 percent of gross value added in the EU -<sup>48</sup>. The European transport sector is still far from being economically and environmentally sustainable. Economic development so far was closely linked with increasing demand for mobility but the current development path in transport cannot be continued without disproportionate societal costs in the long run. In the pursuit of a more sustainable transport system, the challenge does not only lie in infrastructure investment and greener vehicle technologies but a push towards more effective management e.g. as a consequence of stricter pricing and regulatory policies (e.g. in order to lower the share of empty runnings in road freight transport).

There is the challenge of interfaces for the increasingly required seamless door-to-door transport chains, be they for passengers or freight. The interfaces are between the Member States with still differing regulatory frameworks and national standards, e.g. in the rail sector (issue of interoperability) or between private and public organisations in a sector marked by increasing division of labour in many respects, e.g. between usually state-owned infrastructure and operations by publicly or privately owned carriers. Relevant issues are discriminatory behaviour and abuse of market power paired with differing national regulatory regimes and standards.

A pertaining challenge is safety and security. Although the situation has hugely improved over the past 20 years, still almost 30,000 EU citizens die every year in road accidents<sup>49</sup>. Ships and trains transporting dangerous goods can cause

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<sup>45</sup> Cf. Regulation (EU) 1301/2013, Article 3.

<sup>46</sup> In February 2014, the EC adopted new guidelines on state aid to airports and airlines (Aviation Guidelines).

<sup>47</sup> [http://europa.eu/rapid/press-release\\_MEMO-13-448\\_en.htm](http://europa.eu/rapid/press-release_MEMO-13-448_en.htm)

<sup>48</sup> EU Transport in Figures – Statistical Pocketbook 2014.

<sup>49</sup> EU Transport in Figures – Statistical Pocketbook 2014.



catastrophes in case of accidents. Air transport is threatened by terrorist attacks and other security issues.

Infrastructure pricing remains a challenge for the transport sector. Transport infrastructure is usually financed and run by the public sector, state companies or PPP with operations either mostly private (road, deep and short sea shipping), partly private and partly public (inland waterways, air) or predominantly public (rail). Current infrastructure pricing level is only sustainable with heavy public subsidising (road, rail, port infrastructure), sometimes cross-subsidising (e.g. between private cars and lorries on toll motorways). Due to high external costs, prices do not function as signal of scarcity. However, the “user pays” or “polluter pays” principles that are on the one hand side required by principles of fairness and correct allocation of resources in a market economy, would on the other hand side probably induce an abrupt and radical change with unpredictable consequences in the whole economic fabric of Europe when actually implemented on a large scale.

There is a certain trend of focusing on technical innovation in the transport sector, mostly with a background of increased energy efficiency; however, also low-cost technical solutions as well as organisational and commercial innovations play a major role.

A geostrategic perspective shows the challenge of autonomy of the EU or its Member States and regions in globalised transport chains where decisions predefining the intra-European transport flows (e.g. on ports of call) may be taken elsewhere. Not to forget the high dependency of Europe on intercontinental transport flows of raw material, fossil fuels, food imports outside EU territory.

### Perspectives for LRAs

The TEN-T network is marked by corridors and nodes in all transport modes. The network has an evident territorial dimension and among the TEN networks the transport network is the one with the most immediate and strongest impact for LRAs.

It is evident that primarily the development of nodes bears significant opportunities for LRAs – projects on the expansion of hubs – be it multimodal railway terminals, airports, river ports or seaports - are usually cornerstones of strategies at local and regional level. Depending on the political-administrative system of the MS the role of LRAs goes far beyond planning and/or regulatory policies but can reach as far as ownership and management of infrastructure (such as is the case for many airports, riverports and seaports).

Given the fact that these are large-scale transport infrastructures it is evident that environmental concerns and local acceptance have a strong impact on the lead-in time in case of major network extensions. Projects on the expansion of corridors or hubs such as airports encounter increasing public resistance. The sensitive point is local and regional acceptance: planning is – depending again on the political-administrative system either predominantly a central competence or it involves also LRAs – in the latter case it can be ranked among one of the rather demanding challenges for MLG. In particular when speaking of road transport one may also not forget that the access roads to the corridors fall in many MS in the competence of the LRA and bear also significant opportunities in terms of site development but might also increase the risk of uncoordinated sprawl of settlement areas.

From a territorial perspective it is a crucial question at which scale the TEN will contribute to cohesion. Given the investment focus on the inevitably wide-meshed structure of TEN-T and similar approaches, it remains to be seen whether also regions other than agglomeration will draw major benefits. With the exception of regional port and airport infrastructure projects, TEN-T funding concentrates on the challenge of connection with the large centres of the EU but not the challenge of everyday short-to-medium distance transport within the regions. Even with its differentiation between core and comprehensive network, the approach focuses on expanding high-grade infrastructure resulting in a relatively loosely woven network, especially for the most important transport mode, road transport.

Given the budgetary constraints in a mid- to long-term perspective in an EU that is still reeling from the after effects of the financial crisis the role of Community funding for infrastructure investment is decisive in particular for Cohesion Countries. Most of the challenges related to regional development may be significantly influenced by the transport sector (competitiveness and cohesion, sustainable urban development through integrated concepts, tackling climate change and greening the economy). This in turn increases the responsibility of all relevant levels – from the European level to the cities and regions – to maximise the beneficial effect of transport infrastructure investments.

## **Energy**

### ***Major trends in a nutshell***

The EU still depends largely on fossil energy sources (74.6 percent of gross energy consumption)<sup>50</sup>. The energy mix of the EU-28 consists of 34 percent petroleum and products; 23 percent gas; 17 percent solid fuels; 14 percent nuclear; 11 percent renewable (growing from 5 percent in 1995)<sup>51</sup>. The energy

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<sup>50</sup> EU Transport in Figures – Statistical Pocketbook 2014.

<sup>51</sup> EU Energy in Figures – Statistical Pocketbook 2014.

mix is widely varying between the individual MS being determined by geographical, geological, technological conditions, by local energy policies and by national requirements. A base load of fossil energy, nuclear energy and some renewable sources like hydropower or solid biomass is complemented by a variable load of flexible fossil sources and weather-dependent renewable sources currently subject to fluctuations.

The EU-28 increasingly depends on energy imports. It imports 53.4 percent of its energy (2012) as opposed to 43 % in 1995. The EU-28 imports 86.4 % of its petroleum and petroleum products; 65.8 percent of its natural gas; 42.2 percent of its solid fuels. Main countries of origin are for crude oil Russia (34 percent), Norway (11 percent), Saudi Arabia (9 percent), Nigeria (8 percent); for natural gas: Russia (32 percent), Norway (31 percent), Algeria (13 percent) and for solid fuels: Russia (26 percent), Colombia (24 percent), USA (23 percent).<sup>52</sup> The three most important energy sources are highly dependent on imports from potentially unstable countries: Russia is the most important trade partner with one quarter to one third of all imports; also Saudi Arabia (oil), Nigeria (oil), Algeria (gas), Colombia (solid fuels) play crucial roles. Especially for gas, import dependency will rise in the future because of depletion of European resources<sup>53</sup>.

Main consumers (final energy consumption 2012) of energy are transport with 32 (road transport alone accounts for 26 percent; air 4.4 percent), industry (26 percent), households (26 percent) and agriculture (2.3 percent). The distribution has shown a marked change over the past 25 years with transport replacing industry as main consumer (1990: industry 34 percent; transport 26 percent; households 25 percent; agriculture 3 percent) with total energy consumption remaining almost the same 1990-2012. The figures reflect certain trends like increasing division of labour in a globalised economy requiring longer freight transport routes, changes in mobility patterns, the deindustrialisation of large parts of Europe.

Forecasts predict a stable to slightly increasing energy demand until 2030. It is estimated that EU-28 gross electricity generation will grow by at least 20 percent from about 3,362 TWh in 2007 to ca. 4,100 TWh in 2030 whereas gas demand will remain stable and demand for oil and solid fuel will sink.<sup>54</sup>

### *Trends in infrastructure development*

EU electricity grids need modernisation in order to meet increasing demand due to a major shift in the overall energy value chain and mix and the multiplication of applications and technologies relying on electricity as an energy source (e.g.

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<sup>52</sup> EU Energy in Figures – Statistical Pocketbook 2014.

<sup>53</sup> COM 677/2010, p. 21.

<sup>54</sup> COM 677/2010, p. 19-22.

heat pumps, electric vehicles, hydrogen and fuel cells, ICT). The network also has to be upgraded in order to integrate electricity generated from dispersed renewable sources through improved connections and smart grid technologies including large-scale storage. In a horizon up to 2050, new high-voltage long distance and new electricity storage technologies will be required<sup>55</sup>. The priority corridors defined by the EC are the offshore grid in the Northern Seas and its connection to North as well as Central Europe, interconnections in South West Europe for integrating renewable energy sources (esp. France, Spain), connections in Central Eastern and South Eastern Europe strengthening the regional network and the Baltic Energy Market Interconnection Plan (BEMIP) improving the integration of the Baltic States<sup>56</sup>.

Natural gas plays a major role in the EU energy mix, increasingly as back-up fuel. In order to secure its supply and reduce single-source dependency, especially in Eastern Europe, bi-directional pipelines, enhanced storage capacities and flexible supply, including liquefied (LNG) and compressed natural gas (CNG) shall enable a diversified portfolio of physical gas sources and routes and a fully interconnected and bidirectional gas network<sup>57</sup>. The aim is to build the infrastructure needed to allow gas from any source to be bought and sold anywhere in the EU, regardless of national borders.<sup>58</sup> Priority corridors in the gas network have been defined with the Southern Corridor bringing gas from the Caspian Basin, Central Asia and the Middle East to the EU, the Baltic Energy Market Interconnection Plan (BEMIP) and the North-South Corridor in Western, Central Eastern and South-East Europe<sup>59</sup>.

The future network development of crude oil and petroleum product transport infrastructure will be determined by issues of security of supply and future developments in the European refining sector<sup>60</sup>. Priority is safeguarding crude-oil supplies to land-locked EU countries in Central-Eastern Europe by reinforcing the interoperability of the existing Central-Eastern European pipeline network via interconnecting the different systems, removing capacity bottlenecks respectively enabling reverse flows<sup>61</sup>.

“Intelligent” smart grid technologies shall enable a competitive market via the integration of renewable and distributed generation and the accommodation of new types of demand like electric vehicles<sup>62</sup>.

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<sup>55</sup> COM 677/2010, p. 6.

<sup>56</sup> COM 677/2010, p. 10.

<sup>57</sup> COM 677/2010, p. 6-7.

<sup>58</sup> COM 677/2010, p. 11.

<sup>59</sup> COM 677/2010, p. 11.

<sup>60</sup> COM 677/2010, p. 7.

<sup>61</sup> COM 677/2010, p. 11.

<sup>62</sup> COM 677/2010, p. 11.

## The challenges

The energy infrastructure in the EU has to be adapted to provide sufficient capacity for future energy demand, to ensure security of supply and to enable the large-scale deployment of energy from renewable sources. This includes innovative transmission technologies for electricity allowing for large-scale integration of renewable energy, of distributed energy sources, demand response in interconnected networks and innovative transmission technologies for gas providing advanced capacity or increased flexibility allowing for short-term trading or back-up supply. Investment requirements are estimated at 140 BEUR for electricity networks and 70 BEUR for gas<sup>63</sup>. A higher share of renewable in the energy mix increases the risk of natural fluctuations that would have to be compensated by measures like modernising existing and building new power stations, expanding storage technologies as well as expanding transmission and distribution systems. According to the Innovation and Networks Executive Agency (INEA), 60-70 BEUR of the required investment are at risk without public support, because the projects are not commercially viable under current market conditions and regulatory framework, e.g. projects concerning security of supply or solidarity<sup>64</sup>.

Encouraging private investment requires a stable and predictable regulatory framework combined with incentives for projects of common interest. The preamble of the TEN-E regulation hints at some of the potential conflicts connected with investment in energy infrastructure, like public interest potentially overriding concerns on environmental impact or the potential conflict between streamlined and improved permit granting procedures in order to attract private investors (one-stop-shops) and national competences and procedures for the construction of new infrastructure, exigencies on public participation and transparency<sup>65</sup>.

Costs for development, construction, operation and maintenance of energy infrastructure are to be recovered via tariffs according to the user-pays principle in an integrated internal energy market. The tariffs shall provide incentives for investment, while not imposing a disproportionate burden on the consumers.

The fact that fossil fuel will play a crucial role in the foreseeable future and the global competition for access to fossil energy sources leads to geostrategic challenges calling for the provision of alternative supply and transit routes as

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<sup>63</sup> [http://inea.ec.europa.eu/en/cef/cef\\_energy/](http://inea.ec.europa.eu/en/cef/cef_energy/).

<sup>64</sup> [http://inea.ec.europa.eu/en/cef/cef\\_energy/](http://inea.ec.europa.eu/en/cef/cef_energy/).

<sup>65</sup> Regulation (EU) No 347/2013 of the European Parliament and of the Council of 17 April 2013 on guidelines for trans-European energy infrastructure and repealing Decision No 1364/2006/EC and amending Regulations (EC) No 713/2009, (EC) No 714/2009 and (EC) No 715/2009.

well as fostering renewable energy sources. The energy isolation of some Member States can be mitigated by interconnecting networks across borders.

As for transport, safety and security play a crucial role since energy facilities can cause potentially devastating consequences in case of failure, physical attacks or cyber-attacks. The potential consequences imply jeopardised security of supply with adverse effects on the economy as a whole, but also disasters in case of nuclear power plants or large hydro-power plants.

### Role of EU

Since the Treaty of Lisbon (2007/2009), EU energy policy has a basis in Primary Law—TEN-E have a decisive role in ensuring the functioning of the energy market, ensuring energy supply and promoting the interconnection of networks.<sup>66</sup>

According to TFEU Art. 194, it is the right of the Member State to determine the conditions for exploiting its energy resources, to choose between different energy sources and to define the general structure of its energy supply. The levels of involvement differ among the Member States; in some nationalised energy sectors prevail, while in others the role of the state is restricted to regulatory politics.

The long-term EU energy strategy has three main targets<sup>67</sup>:

- sustainability: contributing to the EU's wider social and climate goals combat climate change,
- security of supply: ensure the uninterrupted physical availability of energy products and services on the market and mitigate the external vulnerability of the EU due to its high dependency on imports of fossil fuel,
- competitiveness: foster economic growth and employment via competitive energy supply at a price which is affordable to all consumers, private and industrial.

There is no prioritisation of the three potentially conflicting goals. There seems to be an implicit assumption that measures to reach the three goals will support each other mutually. The five priorities of the Energy 2020 strategy add the aspects of a pan-European integrated energy market, consumer protection, safety

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<sup>66</sup> According to Article 194, TFEU.

<sup>67</sup> COM 639/2010 Energy 2020, p. 2. TFEU Art. 194.

and security and energy technology and innovation to energy efficiency and strengthening the external dimension of EU markets<sup>68</sup>.

The TEN-E priority corridors focus on electricity networks, gas networks and the transportation infrastructure for oil, natural gas, carbon dioxide and bio methane (see above). There is a three-step logic in investment with EU financing only backing up if private investment or regulatory solutions fail.

### Perspectives for LRA

LRA are facing a wide range of challenges on the energy sector but the specific aspect of TEN-E usually leaves less room for the development of active investment strategies. It is increasingly challenging for LRAs to ensure public acceptance for energy corridors in particular when it comes to electricity. A general strategy is the bundling of infrastructures such as TEN-E and TEN-T since otherwise lead-in time for major projects can be long to unpredictable due to public resistance (thus being a clear disincentive for leverage of private funding).

However there is – similar to TEN-T - also the main point of access or feeder lines to main corridors where planning is quite often in the hands of LRAs. These parts of the network are strongly linked to energy strategies at level or LRAs in particular in connection with the requirements caused by the expansion of renewable energy production: at regional scale it requires new infrastructure enabling a multitude of new, decentralised producers to feed energy into the system. Technological challenge is the development of smart networks at local/regional level connecting end-user prices via EDP-based load management to production and demand providing an incentive for energy efficiency and aligning decentralised production and decentralised consumption. Such networks can be financed with ESIF support.

Issues of security of supply prevail in peripheral or geographically disadvantaged regions with questions like energy self-sufficiency of outermost regions.

### **Telecommunication**

The telecommunication sector is mainly characterised by rapid technological development leading to a certain tendency of oligopoly or monopoly markets. In order to evening out gap between incumbents and newer rivals, open-access broadband networks with horizontally layered network architecture and business

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<sup>68</sup> COM 639/2010 Energy 2020.

model separating physical access to the network and service provision are favoured.

Challenges in the sector are security and protection of personal data, the transition to fibre networks in order to offset the rising copper price, better use of existing infrastructure and the introduction of next generation networks for transporting all kinds of information and services. The introduction of e-Government raises issues of interoperability of public administration.

The EU strategy as laid out in the Digital Agenda (2010) defines its action areas as:

- Digital single market.
- Interoperability and standards.
- Trust and security.
- Fast internet access.
- Research and innovation.
- Enhancing digital literacy, skills, inclusion.
- ICT-enabled benefits for the society in specific sectors (health, environment, culture, government, transport<sup>69</sup>).

TEN priorities comprise the development of EU wideband networks ("information highways") and the creation of telematics networks between government departments especially in the fields of customs, indirect taxation, statistics and border checks. Further fields of activity are access to public sector information (PSI) and multilingual services, safety and security as well as smart energy services.

The idea is that the private sector should play the leading role in rolling out and modernising broadband networks, supported by competitive and investment-friendly regulatory framework. Where private investment falls short, Member States should make the necessary efforts. The financial instruments used should not distort competition, crowd out private investment or create disincentives for private operators. Based on an ex-ante assessment, EU financing mechanisms are intended to help attracting additional investment, providing a multiplier effect and facilitating the efficient use of private and other public investment.

### Perspective for LRAs

From the perspective of LRAs fast and operationally reliable communication links and efficient wireless mobile services play a role of paramount importance for regional competitiveness, accessibility and equality. There is a need for

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<sup>69</sup> A Digital Agenda for Europe, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, 26.08.2010.



public investment in links between network nodes in middle-sized cities and small towns or rural municipalities helping to ensure equal, affordable broadband access in areas where the market fails. The task is to stimulate public and private investment for rural, low-density, outermost areas. One possibility could be PPP for between LRA and local innovative SME for public services, broadband networks or content digitisation.

### **2.2.6 SME policy**

In general SME-policy is multi-faceted and spans from regulatory policies over education to the role of public intermediaries such as Business Agencies or public procurement and investment support. This specificity of SME-policy - in sharp contrast to other policies which are in hands of or dominated by public actors firmly anchored in traditional patterns of competences – points at one of the major underlying challenges: the issue of policy coordination which has a horizontal and a vertical dimension. An effective and efficient approach to SME policy in a global economy is a vital challenge calling for dedicated action from the public sector.

#### *Key role of SMEs in the EU economy and major trends*

Micro-enterprises and SMEs (defined as having less than 250 employees) are considered as the engine of the European economy. Over 90 percent of EU businesses are SME, in total more than 21 million Euros in 2013; they provided 88.8 million jobs, generating two thirds of all private sector jobs. They show double the employment growth rate of large enterprises<sup>70</sup>.

However, as the European Commission pointed out in its “Small Business Act”, their 2008 strategy paper outlining future EU SME policy, Europe is lagging behind other, more dynamic parts of the world. In the USA, SMEs show higher productivity and faster growth than in the EU and have much higher employment gains a few years after their establishment<sup>71</sup>. SMEs in Europe face a number of challenges preventing them from realising their full potential as growth engine for the continent.

#### *Major challenges*

SMEs are more sensitive to the regulatory and administrative burden of entrepreneurship than large companies. It is estimated that an SME on the average has ten times the costs per employee on regulatory duties as a large enterprise<sup>72</sup>. Taxes, duties and other charges pose additional obstacles,

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<sup>70</sup> EC 2015 p. 3.

<sup>71</sup> EC 2008 p. 3.

<sup>72</sup> EC 2008 p. 7.

especially for newly established businesses. Common provisions like minimum corporate taxation, minimum social insurance fees or minimum share capital requirements can pose serious problems to start-ups (and may even be considered as discriminatory); they can easily have prohibitive effects. One reason for the weaker growth of European SMEs as compared to their counterparts may simply lie in the difference of the total tax burden ('tax wedge') on labour income. OECD average for a single person with an average wage in the private sector is 36 percent<sup>73</sup>, as compared to 39 percent in EU-28<sup>74</sup>. The only EU MS below OECD average are PL (35.6 percent), the UK (31.1 percent) and IE (28.2 percent)<sup>75</sup>. However, many fiscal incentives tend to benefit only taxable firms but do not necessarily include loss-making ones (like many start-ups) or those about to be established.

Difficulties with access to finance – one of the major constraints for SMEs – arise from high risk of entrepreneurial activities and information asymmetries between investors and entrepreneurs. As the OECD points out, in the period 2007-2010 credit conditions were stricter for SMEs than for large enterprises (higher interest rates, shortened maturities, higher collaterals). The financial crisis and the sustained high uncertainty in the banking environment (structural weaknesses in the Euro banking sector, Basel III reforms etc.) have widened the gap<sup>76</sup>. Governments – as a reaction to the aftermath of the crisis – have injected money in their direct lending and loan guarantee programmes with varying focus (e.g. AT seed financing for young firms; HU massive enlargement of loan guarantee programme DK new programme with subordinate loans etc.) but also conventional debt funding such as the British Business bank which will administer the Enterprise Finance Guarantee for SMEs<sup>77</sup>. New approaches such as Peer-to-Peer (P2P) lending or crowd funding have seen rapid increase but remain marginal<sup>78</sup>.

Access to public procurement, representing between 15 and 20 percent of EU GDP<sup>79</sup>, can pose serious problems for SME, starting with insufficient information, continuing with requirements of track records or minimum yearly turnover, costly proposals required and ending with slow and cumbersome payment by public bodies causing severe liquidity problems or even bankruptcy with SME.

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<sup>73</sup> E.g. USA 31.5 %, Canada 31.5 %, Korea 21.5 %, Australia 27.7 %.

<sup>74</sup> E.g. France 48.4 %, Germany 49.3 %, Italy 48.3 %, Spain 40.7 %.

<sup>75</sup> <http://stats.oecd.org/>

[http://ec.europa.eu/eurostat/statistics-explained/index.php/Wages\\_and\\_labour\\_costs#Tax\\_wedge](http://ec.europa.eu/eurostat/statistics-explained/index.php/Wages_and_labour_costs#Tax_wedge).

<sup>76</sup> OECD, 2014 p. 73.

<sup>77</sup> OECD 2014, p. 162.

<sup>78</sup> OECD, 2014 p. 73.

<sup>79</sup> EC 2012 p. 9.

A severe problem identified by the Small Business Act is how to give undertakers having gone bankrupt a new chance (around 700,000 SMEs go bankrupt every year in the EU with almost three million jobs affected). The length of bankruptcy procedures in the Member States varies widely between four month and nine years<sup>80</sup>. Combined with the difficult access to financial means often requiring personal liability of the undertaker for credits, a bankruptcy can all too easily end up in personal ruin.

Entrepreneurial education is another aspect of the complex, as is creating a positive image of entrepreneurship, especially with pupils and students. Lack of required skills on the labour market poses a challenge, as has shown a public consultation cited in the Small Business Act where 60 percent of companies complained that schools do not provide the competences needed by the entrepreneurs. Research and innovation can be considered a weakness of many SME. Less than one third of European SMEs generate income from new products.<sup>81</sup>

Internationalisation is a main challenge for SME who are often not able to reap full benefit from the Single Market. Integration of SMEs to Global value Chains (GVCs) is vital – access for SMEs to knowledge flows and knowledge hubs is crucial but an inherent challenge for small businesses with limited capacities.

### Policy responses

Policies facilitating market entry are crucial: this refers in particular to competition policies, taxation and a wider notion of labour-market policies (labour cost, non-wage labour cost, social insurance entitlement). After the crisis many countries have simplified business regulations<sup>82</sup>.

Fostering new firm foundation is a key objective of SME policy throughout the EU – a broad range of approaches exist: skills development (entrepreneurship education, VET, advice on business creation – mentoring, coaching etc.), entrepreneurship programmes (e.g. awareness-raising campaigns, award programmes, support programmes fostering self-employment, combination of advice and financial instruments such as interest rate subsidies, loans, grants, income subsidy schemes etc.). Recently, a new focus on services has been developed - the growing role of services has been neglected over a long period in such programmes.

Most MS are trying to foster the internationalisation of SMEs with instruments such as Technology Partnerships in UK a dedicated support tool to help

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<sup>80</sup> EC 2008 p. 7.

<sup>81</sup> EC 2008 p. 15.

<sup>82</sup> OECD 2014, p. 179.

knowledge-intensive SMEs to identify supply-chain opportunities of global companies.

### Role of EU

The overarching policy approaches at EU level are mainly focussed on a reform of the regulatory environment and programmes for the stimulation of SME development. Examples are the Financial Instruments Directive (MiFID)<sup>83</sup> which will create dedicated trading platforms labelled "SME growth markets" or the Capital Requirements Regulation including a correcting factor lowering the capital requirements.

The Small Business Act for Europe (SBA; adopted in June 2008) established for the first time a comprehensive SME policy framework for the EU and its Member States reflecting the Commission's political will to recognise the central role of SMEs in the EU economy<sup>84</sup>. The SBA has been subject of a review in 2011<sup>85</sup> and the current debate goes towards the SBA 2.0. The Single Market Act is an initiative which gained momentum in 2010 in the wake of the economic crisis and the persistent economic and social problems in the crisis' aftermath. The overarching strategic aim is to make the Single Market a tangible reality for businesses and citizens.<sup>86</sup>

The SMA is not one Act but a set of interlinked key policy areas. It is also an ongoing reform agenda: for many of these policy areas legislative proposals have been developed, negotiated and adopted. The SMA II puts particular emphasis on sectors with large growth potential, i.e. services and networks. Based on assessments of production benchmarking, economic importance, dynamic factors and single market factors four major areas have been identified where improvements *could harness untapped potentials*.<sup>87</sup> The four drivers for new growth put forward in this Communication are:

1. Developing fully integrated networks in the Single Market;
2. Fostering mobility of citizens and businesses across borders;
3. Supporting the digital economy across Europe;
4. Strengthening social entrepreneurship, cohesion and consumer confidence.

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<sup>83</sup> In force since 2007 this directive governs the provision of investment services in financial instruments by banks and investment firms and the operation of traditional stock exchanges and alternative trading venues; shortcomings in the wake of the crisis have led to MiFID II in 2014.

<sup>84</sup> Cf. COM 2008 (394), Small Business Act.

<sup>85</sup> Cf. COM 2011 (78), Review of the Small Business Act for Europe.

<sup>86</sup> Cf. COM 2012 (573), Single Market Act II.

<sup>87</sup> Cf. COM 2012 (259), p. 13.

EU Cohesion Policy as one strand of SME investment policy plays a major role as public investment policy. In the SF period 2007-2013 nearly € 70 billion or 20percent of the € 346 billion take the form of direct support to companies through grants, business services, loans, guarantees or equity stakes<sup>88</sup>. The support is granted mainly under three headings:

- Innovation and R&D (€ 26.3 billion of ERDF or 7.7percent of all cohesion policy funding).
- Other SME and Business support:(€30.7 billion of ERDF or 8.6percent of the total) is predominantly benefitting SMEs including measures approved under regional (notified) aid schemes, R&D&I, environment and risk capital guidelines, access to finance through financial engineering instruments (loans and guarantees).
- Labour Market in firms: (€ 12.7 billion or 3.7percent of the total) mainly from the ESF.

#### *Key dimensions of SME policy in relation to EU Cohesion Policy*

SME policies need to be considered as a multi-faceted policy which should include a number of policy angles. The following table is based on the OECD's notion of major dimensions in SME policies<sup>89</sup>- which is closely related to the principles of the SBA. The table seeks to establish the relation to interventions in the frame of Cohesion Policy.

**Table 14. Major dimensions of SME policy in relation to EU Cohesion Policy**

<b>Dimension of SME policy</b>	<b>Relation to EU Cohesion Policy</b>
Institutional and regulatory policy framework (SBA principles I, III& IV)	No direct impact of EU CP on crucial aspects such as taxation but for evident reasons the leverage of most CP interventions strongly relies on a sound economic development
Standardisation, patents, trademarks, IPR as keys to the Single Market (SBA principle VII)	No direct impact of EU CP
Access to finance (SBA principle VI)	Counterbalancing role through SME support programmes and increasing role of financial instruments under ERDF – however, given the magnitude of the challenge the volume of interventions from ERDF is marginal

<sup>88</sup> EC 2013, pp. 6-7.

<sup>89</sup> OECD 2014a), p. 13.

Education and training for entrepreneurship (Entrepreneurial education at school; collaboration between higher education and business etc.) (SBA principle I)	Visible role of the ESF but the bulk of ESF-funding goes to active labour market policy (with an increasing focus on poverty reduction)
Operational environment for business creation (registration and administration linked to set-up of businesses) (SBA principle I)	No direct relevance of EU CP
Support services for SMEs (SBA principle IV)	In many countries strong role of intermediaries such as business agencies in ERDF programmes (from participation in programming to implementation in the function of Intermediate Bodies)
Enterprise skills and innovation (SBA principle VIII)	Policy focus with an increasing role in ERDF
Internationalisation of SMEs; (SBA principle X)	Programmes for internationalisation of SMEs are often co-funded from ERDF
Public procurement (PP) (SBA principle V)	SF and ESIF account for significant shares of public investment in particular in EU12/13 – this has been and will be a key market for SMEs (in particular in times of crisis and decreasing private consumption)
Efficient bankruptcy and second chance for entrepreneurs (SBA principle II)	No direct relevance of/for EU CP
Greening the economy (eco-efficiency and eco-innovation) (SBA principle IX)	Strong relevance in CP: focus of CP (IP 4); major focus of STI in EU

*Source: OECD 2014a), SBA, own considerations.*

A recent study for the European Parliament<sup>90</sup> has outlined key obstacles for SMEs related to EU CP. The study has identified several issues which pinpoint the need for action in ESIF programme management. The three most important are:

- Need to reduce the number and complexity of administrative requirements for SF (ESIF).
- Need to open SFs to new SMEs as entrants (since the offers under SF tend to be used by applicants with previous expertise).
- Speed-up the decision-making process in many MS in order to make the support a reliable part of any business or investment plan.

Generally speaking it is important to note that the implementation of the programmes under SF/ESIF is in the hands of the MS – thus these major

<sup>90</sup> CSIL, PPMI 2013, pp. 16-17.

criticisms from the perspective of SMEs refer firstly to the implementation practice of the MS. One of the major recommendations of the study is to rely more strongly on financial instruments in SME-support as part of CP: these instruments are more akin to business practices of SMEs and the corresponding administrative burden is generally lower than for grants. However, the set-up of financial instruments is perceived as a significant challenge for the programme management since such instruments entail cooperation with new players such as banks and new routines in particular in risk assessment and management.

### Further major SME-related investment initiatives at the European level

The Competitiveness and Innovation Programme (CIP) had assisted financial institutions in providing about EUR 30 billion of new finance for more than 315 000 SMEs and have created or maintained directly about 380 000 jobs<sup>91</sup>.

COSME is an EU programme for the Competitiveness of Enterprises and Small and Medium-sized Enterprises (SMEs) running from 2014 to 2020 with a planned budget of €2.3bn focusing on supporting entrepreneurs, better access to finance for SMEs, access to markets and more favorable conditions for business creation and growth<sup>92</sup>.

The new SME Instrument of Horizon 2020 targets the innovation weaknesses perceived with SME<sup>93</sup>.

### Perspective of LRAs

In general the major policies which have a decisive role in framing SME development are in the hands of institutions at the national level: these have to be considered mostly as regulatory policies such as taxation and labour market policies<sup>94</sup>. Generally speaking the lever of direct monetary support to SMEs is restricted: the state aid rules clearly limit the scope of direct financial support. Those regions which reveal the most dynamic developments – i.e. the urban agglomerations - are those where possible support rates are the lowest (and low support rates further the tendency towards windfall gains without effectively influencing decision-making).

SME policy and in particular direct support to SME investment is one of those areas where major differences across MS become visible:

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<sup>91</sup> EC 2014, p. 17.

<sup>92</sup> [http://ec.europa.eu/enterprise/initiatives/cosme/index\\_en.htm](http://ec.europa.eu/enterprise/initiatives/cosme/index_en.htm).

<sup>93</sup> <https://ec.europa.eu/programmes/horizon2020/en/h2020-section/sme-instrument>.

<sup>94</sup> In this case understood as those policies which in the end define the cost of labour for entrepreneurs.

- In parts of the ‘old’ EU many MS have a tradition of SME policies, in federal countries such as AT, DE or IT programmes for SME support exist at regional and in case of larger cities even at local levels – quite often programmes for SME-support at regional level mirror or complement programmes at national level; in such countries in the end a broad variety of instruments is offered ranging from grants over subsidised loans to seed financing; policy coordination between national, regional and eventual local programmes increasingly becomes an issue (embedded in a general debate on the effectiveness of such measures).
- In most of the EU 12/13 the approach to SME policy with a major funding element has been established after EU accession – the approach is usually strongly centralised and mostly based on grants for investment activities.

Next to direct SME-support a broad range of support instruments at level of LRAs has been established. These instruments can be understood as intermediaries which step in between public actors and entrepreneurs. Such instruments usually comprise consultancy and mentoring eventually combined with infrastructure. The scope of instruments ranges from regional business or SME agencies to incubators or shared offices.

The policy options for SME development at the local level are usually rather limited and for obvious reasons the size of municipalities is decisive:

- Small municipalities focus their SME policies on the provision of sites and facilities such as business parks; this local competition for firms ends often in under- or unused sites due to high numbers of sites without corresponding demand; moreover the development fuels the sprawl of settlement areas
- For cities and agglomerations the policy options are broader and strategies can combine direct investment support with the potentialities of specific education facilities plus interesting sites (such as former industrial real estate) and further factors to attract SMEs or specific groups of micro- and small businesses<sup>95</sup>

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<sup>95</sup> There are e.g. interesting examples of such site development in old industrialised cities in DE, FR, ES, UK – targeting young firms as key element to actively foster the process of economic restructuring; also programmes for urban renewal in deteriorated areas usually include inter alia the support to small or micro businesses.



## 2.3 Policies for specific regions

Despite the evident dominance of sectorial approaches in most MS the aspect of the policy focus on specific regions must not be forgotten. In part the EU provisions for Cohesion Policy do foresee or shape incentives in that sense. In part some MS have such approaches which have been / are being reinforced by EU Cohesion Policy. The sixth Cohesion Report shows that in the 2014–2020 period, a new measure has been introduced facilitating the use of functional geography: integrated territorial investment which is intended to make it easier to implement an integrated strategy in a specific area, such as a metropolitan area or a cross-border area. To obtain a better understanding of the functional geography dimension, the Commission has developed a number of new harmonised territorial definitions:<sup>96</sup>

- Together with the OECD, it has created a new harmonised definition of a city and its commuting area, which shows that the latter, especially in large cities, often cross NUTS 2 boundaries and even national borders.
- Combining the approach used for the urban-rural regional typology developed in 2010 and the new city definition, it has also defined a new local typology, the degree of urbanisation, which distinguishes rural areas, towns and suburbs, and cities. This allows for a better monitoring and understanding of the different policy issues facing all types of area, rural as well as urban.

To give these local and regional typologies more stability and visibility, the Commission intends to include them in an annex to the NUTS regulation.

However, already the fifth Cohesion Report used six regional typologies based on NUTS-3 data or lower as presented in the table:

**Table 15. Regional typologies used in the 5th Cohesion Report**

Regional typologies	Classification	Scope
urban-rural typology including remoteness	classifies all NUTS-3 regions according to criteria based on population density and population distribution (including capitals); combined with a distinction between areas located close to city centres and areas that are remote	EU-wide (+ NOR, CH, LIE, ISL)
Metro regions	grouping of NUTS-3 regions used as approximations of the main metropolitan areas	Agglomerations in the whole EU area (excludes peripheral regions in Northern Scandinavia, ES, PT, FR, IT, GR, etc.)

<sup>96</sup> Sixth Cohesion Report, p. 202.

Border regions	<b>Internal border regions:</b> located on borders between EU Member States and/or European Free Trade Area (EFTA) <b>external border regions:</b> participating in programmes involving countries outside both the EU and EFTA	Core areas of cross-border cooperation
Mountain regions	At NUTS-3 level; defined as regions in which more than 50% of the surface is covered by topographic mountain areas or in which more than 50% of the regional population lives in these topographic mountain areas	NOR, UK, DE, CZ, SK, CH, AT, FR, ES, PT, IT, SI, HR, RO, BG, GR
Island regions	NUTS-3 regions entirely covered by islands. They can correspond to a single island, can be composed of several islands, or can be part of a bigger island containing several NUTS-3 regions	EU Islands
Sparsely-populated regions	NUTS-3 regions with a population density of fewer than 12.5 inhabitants per km <sup>2</sup>	Northern Scandinavia, Island, Northern UK, Central ES, Parts of HR GR and Turkey

Source: own preparation based on Dijkstra, Lewis and Hugo Poelman 2011.

## EU regulations on policy for specific regions

Within the current financial framework (2014-2020) spending on Cohesion Policy amounts to one third of the total EU budget. According to the Lisbon Treaty the European Union should promote not only economic and social but also territorial cohesion. This implies the aim to ensure a more balanced development of economic activity across all of its regions including urban and rural areas, islands and peripheral regions as well as mountainous regions.

A starting point for analysis is Art. 174 (FTEU) mentioning the “aim at reducing disparities between the levels of development of the various regions and the backwardness of the least favoured regions.” It is further specified that “particular attention shall be paid to rural areas, areas affected by industrial transition, and regions which suffer from severe and permanent natural or demographic handicaps such as the northernmost regions with very low population density and island, cross-border and mountain regions.”

“Key territorial challenges for urban, rural, coastal and fisheries areas, demographic challenges of regions or specific needs of geographical areas which suffer from severe and permanent natural or demographic handicaps” are also addressed by the Common Strategic Framework<sup>97</sup>.

<sup>97</sup> Art. 10 Common Provisions (CPR)(1303/2013).

## The instrumental approaches at European level

Next to a strong emphasis in the overarching documents CP includes also some responses to the challenges for specific types of regions. One of the approaches is the option to modulate the co financing rates according to specific types of regions.<sup>98</sup> The Regulation pinpoints the following ones:

- Island MS which are also Cohesion Countries (MT, CY).
- Mountainous areas defined according to national legislation.
- Sparsely populated (less than 50 inh./sqkm) and very sparsely populated areas (less than 8 inh./sqkm).
- Outermost regions<sup>99</sup> which receive also an extra envelope within the Objective of Investment for Growth and Jobs<sup>100</sup>.

An example of a broad approach to strategies are urban areas. The Commission intends to pay more attention to urban areas. At EU level € 372 million will be dedicated to innovative urban actions<sup>101</sup> that shall include studies and pilot projects to test new solutions to urban challenges that are likely to grow in the coming years. MS are obliged to foresee a minimum of 5% of ERDF to target urban areas with integrated strategies for sustainable urban development.<sup>102</sup> The Integrated Territorial Investment (ITI) as an option for cross-funds or cross-programme interventions has its roots in model strategies for deprived urban areas combining operations under ERDF and ESF.

At European level, cohesion can be considered as narrowing disparities between regions within the EU as a whole. Therefore also indicators such as GDP per capita, median income levels, employment rates and education levels refer to the average values of the whole EU. It is obvious that there is a different consideration of regions and indicators in the MS.

## National policies for specific regions

Member States can only actively contribute to cohesion within national frontiers. However, MS address internal economic, social and territorial disparities in different ways and assign differing priorities to the convergence of regions. According to a study of EPRC<sup>103</sup> large countries are more likely to contain significant internal disparities and more prosperous countries are more likely to have the capacity to address them. Moreover, the study distinguishes

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<sup>98</sup> Art. 121 CPR.

<sup>99</sup> Acc. Art. 349 of TFEU.

<sup>100</sup> 1.3 BEUR – cf. CPR, Art. 92.

<sup>101</sup> Art. 8 ERDF Regulation (1301/2013).

<sup>102</sup> Cf. ERDF Regulation, Preamble, Recital No 19).

<sup>103</sup> EPRC and Euroreg 2010, The objective of economic and social cohesion in the economic policies of Member States.

between four groups of countries in terms of ‘importance given to regional policy’<sup>104</sup> as presented in the table below:

**Table 16. Relative importance of national regional policy**

Importance	Country characteristics	Scope
Limited importance given to regional policy	Small, prosperous countries with limited internal disparities; Less prosperous, small, peripheral, essentially unitary countries with some internal disparities, but a limited recent tradition of regional policy; Large, less prosperous countries with wide internal disparities, but limited recent tradition of regional policy	LU, NL, DK, AT  GR, PT, SK, IE, BG, CZ, EE, HU, LT, LI  PL, RO
Modest importance given to regional policy	Large, relatively prosperous countries with diverse regional challenges; Smaller, less prosperous countries facing a range of diverse internal disparities	FR, UK  MT, SI, CY
Significant Importance given to regional policy	broad and integrated nature of policy, which cuts across and involved coordination with sectoral policy has significant profile and expenditure	SE, FI
Regional policy considered as essential	large countries with internal economic disparities and where the requirement to address regional inequalities is enshrined in the constitution	ES, IT, DE

Source: EPRC and Euroreg 2010.

In response to the crisis, some MS have changed their approach to regional development policies. In BE, DK, FR, DE, PT, ES and UK authorities have improved the accessibility of regional funding, i.e. implementation rules have been simplified or the range of potential beneficiaries extended. On the other hand, funding for regional policy has been cut in some countries (IT, IE, EE, RO, UK) where budgetary pressures have taken effect.

In Germany, €200 million were additionally allocated to the main German regional policy scheme, the ‘Joint Task for the Improvement of the Regional Economic Structure’.

Other countries introduced new instruments that target at the most affected regions (CZ, SI, FR). In France and Sweden specific coordinators have been nominated to oversee the policy response at the sub-national level (*ibid.*).

### **Challenged regions which deserve particular attention**

<sup>104</sup> An exception is Belgium where there is no national regional policy and responsibility for economic development devolved to the regional level (Brussels, Flanders and Wallonia).

The fact that the Regulations mention specific types of regions which deserve particular attention and thus might fall under specific provisions in the implementation of CP can be considered as an important policy lever. However, the development and implementation of tailored and integrated strategies is in hands of the MS. Next to urban regions, three exemplary types of regions should be highlighted:

- Coastal regions.
- Sparsely populated, overseas regions.
- Mountainous regions.

Almost one third of NUTS-3 regions in the EU (incl. NOR, CH, LIE, ISL) are coastal regions that face very different and very specific challenges for human living, economic activities and environmental protection<sup>105</sup> that deserve integrated strategies. Whereas some remote coastal regions experience decline in population, employment and income, others profit from touristic flows which – on the other hand – erode the environmental potential. Regions with harbour functions gain from the growing importance of long and short sea shipping.

Also, specific challenges in sparsely populated, overseas regions that suffer from their physical remoteness require long-term efforts and dedicated interventions at several levels. For those regions, the EU market is far away and not easily accessible which makes it difficult to achieve economies of scale and to generate profits from major investments. The integration into regional organisations and the specific association regimes are at least as important as ‘traditional’ CP interventions. Especially small islands at the European periphery typically face disadvantages in accessibility.

A third, very specific type of regions are mountain regions that are increasingly valuable for recreation and tourism but suffer from population decline and rank among those regions which are most vulnerable to the adverse impact of climate change. Challenges to be tackled refer to the management of international transport, mobility corridors that cross mountain areas and access points to such networks and increasing cost for protection of settlement areas from natural disasters. Again, very diverse pictures result when comparing the Alps close to the economic core areas of the EU with the less accessible and peripheral mountainous regions in Bulgaria and Spain.

Different regional specificities need different strategy implications that have to be met by Art. 174 (FTEU) and the EC’s Green Paper on Territorial Cohesion but also by territorial cooperation programmes. Integrated strategies and multi-fund approaches that are not designed at NUTS-2 or NUTS-3 regions but at the

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<sup>105</sup> ESPON Project 3.1 – ESPON Atlas. Mapping the structure of the European Territory, October 2006.

level of individual islands or valleys as well as functional regions are able to tackle occurring problems.

The scientific debate focuses mostly on the identification of structural constraints and on barriers to development. However, strategies that would make it possible to exploit their potentials and recognise their assets remain to be defined<sup>106</sup>.

## **Practical effects on LRAs**

Those regions which deserve particular attention due to the multi-faceted challenges and the need for integrated strategies would in principle need high governance capacities at level of LRAs. But it is evident that in particular in regions such as fragile island economies or peripheral mountainous regions the LRAs have to face significant economic constraints which usually do have repercussions on the governance capacities. For such regions the implementation of integrated strategies with a strong element of MLG is considered as the ideal policy approach but in practice is rarely found.

At European level the Regulation foresees instruments which do reveal significant potentialities as policy levers for LRAs: these are so-called Integrated Territorial Investments (ITI) and Community-Led Local Development (CLLD). The instruments have been mainstreamed, i.e. introduced in the CPR thus being open for use under all ESIF (cf. chapter 2.1). In principle ITI and CLLD allow tailoring policy responses to the needs of small territories – the rationale of the instruments is the definition and implementation of sub-plans within the framework of an OP. The period 2014-2020 will show to which extent the mainstreaming of the instruments supports a wider use in CP: up to now cross-funding has been rarely used and CLLD was limited to rural development policies under EAFRD. It is obvious that in particular in EU12/13 these instruments could strengthen the governance and strategy-building capacities of LRAs but this will only be possible with the dedicated support from the national level.

Particular policy options arise for LRAs in urban regions respectively for cities by fostering integrated strategies<sup>107</sup> which enhance sustainable urban development. The major advantage for urban regions compared to other types of regions is that urban regions tend to have higher governance capacities partly owing to the manifold public amenities to be managed, partly owing to own statutes stemming from history. With regard to the preparation and management of programmes the implementation of integrated urban development strategies that are able to tackle multiple challenges facing their cities implies the

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<sup>106</sup> ESPON & BBSR, ESPON Atlas 2013. Mapping European Territorial Structures and Dynamics.

<sup>107</sup> Art. 7 ERDF regulation (1301/2013).

delegation of tasks to LRAs. This might deepen the responsibility of LRAs concerning the actual implementation of integrated strategies.

The stronger urban focus in OPs implies not only a thorough territorial analysis to be provided by the MS but could support a tendency to delegate tasks (specifically project selection) to urban authorities.

With the aid of innovative urban actions innovation will be increased and capacity building as well as exchange of experience is expected to be reinforced through the Urban Development Network (UDN)<sup>108</sup> and the financially strengthened URBACT III programme.<sup>109</sup>

## **2.4 Major challenges and trends influencing many policy areas**

Cohesion Policy has to face overarching challenges which provide new angles and have led and will lead to further impetus for policy development. These challenges are usually dominated by global driving forces, which are often beyond the control of the Member States or as the Union as a whole, yet influence the success (or failure) of the policy initiatives or responses.

The European Environment Agency has identified in the SOER 2015 Report<sup>110</sup> a set of 11 thematic fields, namely:

1. Diverging global population trends, with an ageing “first world”, a stabilising Asia and a rapidly growing Africa.
2. A rapidly urbanised global population reaching an urban population which in 2014 accounted for 54 percent of the total global population<sup>111</sup>.
3. Changing disease burdens and risks of pandemics.
4. Accelerating technological change, rise of an information society and of a knowledge economy.
5. A need for continued economic growth.
6. Increasingly multipolar world.
7. Intensified global competition for resources.
8. Growing pressures on ecosystems.
9. Increasingly severe consequences of climate change.
10. Increasing environmental pollution.
11. Diversifying approaches to governance.

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<sup>108</sup> Art. 9 ERDF regulation (1301/2013).

<sup>109</sup> European Commission, factsheet on integrated sustainable urban development.

<sup>110</sup> EEA, 2015, The European environment — state and outlook 2015: synthesis report, European Environment Agency, Copenhagen.

<sup>111</sup> WHO, 2015, Global Health Observatory (GHO) data.

KPMG/MOWAT have in their report on the global megatrends<sup>112</sup> additionally mentioned “Rise of the individual” (12), “Economic interconnectedness” (13) and “Public Debt Dynamics”(14).

Further useful aspects are addressed in ASP Strategy Development Project<sup>113</sup>, namely “Tensions on the energy market” (15) and “Increased mobility of goods and persons” (16).

This list can be enriched ad infinitum; however the set of “Major challenges and trends” seems to be adequate to the scope of the present study.

The Terms of Reference offer a useful set of categories for clustering, namely:

- Economic (crisis);
- Demographic change and migration;
- Climate change expanded by Environment;
- Globalisation / External policies / Tackling of increasing geostrategic risks (with massive economic implications such as the issue of energy sources and other crucial assets).

These categories can be expanded by adding Technological and Institutional aspects<sup>114</sup>.

In the table below they will be presented in a structured way related to the implications for the Cohesion Policy and on the options available for LRAs.

The main questions to be asked in this table are:

- Is the respective global challenge and trend cluster increasing the demand/scope for a Cohesion policy intervention?
- Is the respective global challenge and trend cluster impeding the achievement of the intended benefits of the Cohesion policy intervention?
- What are the implications for LRA?

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<sup>112</sup> KPMG/MOWAT, 2014, Future State 2030: The global megatrends shaping governments, KPMG International Cooperative.

<sup>113</sup> Gloersen et al, 2013, Strategy Development for the Alpine Space - Final Expert Report, Salzburg.

<sup>114</sup> E.g. as in Camagni, R., Capello, R., Spatial Scenarios and orientations in relation to the ESPD and EU Cohesion (2004-2006), ESPON, 2005.



**Table 17. Major challenges and trends influencing CP and LRAs**

Category	Major Challenge and Trend	Effect on Demand/Scope of Cohesion Policy	Effect on Impact of Cohesion Policy	Implications for LRA
<u>Economy</u>	<p>5. <i>A need for continued economic growth</i></p> <p>13. <i>Economic interconnectedness</i></p> <p>16. <i>Increased mobility of goods and persons</i></p>	<p>The pressure on enterprises and especially SMEs is growing, hence the need for specific support (e.g. administrative and tax burden, access to finance, integration in Global Value Chains) will be sustained if not reinforced.</p> <p>It will be necessary to render SMEs competitive on the global market.</p>	<p>The changes imposed by the challenges and trends are materialising much faster than the policy cycle.</p> <p>Cohesion policy can hardly react at this pace.</p> <p>At the same time a “reactive” policy can only have short term effects.</p>	<p>LRA will be exposed to competition for their movable assets and also will have to promote their territorial immovable assets.</p> <p>The provision of high-quality, stable locations are crucial although no guarantee for success. For that reason it will be necessary to be involved in networks and informal forms of cooperation with the business sector.</p>
<u>Demographic change and Migration</u>	<p>1. <i>Diverging global population trends, with an ageing “first world”, a stabilising Asia and a rapidly growing Africa;</i></p> <p>2. <i>Rapidly urbanised global population</i></p>	<p>Demographic dynamics suggest that these trends will be sustained. The demographic decline of Europe will make the integration of migrants inevitable. Hence the demand for employment, education and social inclusion interventions will remain.</p> <p>At the same time the administration will have to depart from static approaches and react dynamically to the needs of migrants and natives.</p>	<p>Social integration will take time to materialise. Hence the balance must be kept between short term preservation of social peace and long term integration.</p> <p>The long term nature of expected effects might lead to mid-term rejection of the policy by the electorate.</p>	<p>LRA will have to promote “grass-root” approaches and local initiatives allowing for a cost effective integration of migrants and of local community acceptance.</p>

<u>Climate Change and Environment</u>	<p>3. <i>Changing disease burdens and risks of pandemics</i></p> <p>8. <i>Growing pressures on ecosystems</i></p> <p>9. <i>Increasingly severe consequences of climate change</i></p> <p>10. <i>Increasing environmental pollution</i></p>	<p>The demand for interventions in the field of environment will be increasing. These will have two dimensions, one regarding hard infrastructure (e.g. sea defences or refuse incinerators) and one regarding intelligent management approaches (e.g. ecosystem management or waste prevention).</p>	<p>Hard infrastructure investments are politically more effective, since more visible. This could lead to a downwards spiral of reacting to hazards instead of reducing them with a steadily decreasing benefit to cost ratio.</p>	<p>LRA will have to focus on flexible operation of infrastructures (according to needs and not demand and considering territorial features and demographic trends, instead of trying to provide “one size fits all” solutions) and intensify cooperation across administrative borders.</p>
<u>Technology</u>	<p>4. <i>Accelerating technological change, rise of an information society and of a knowledge economy</i></p>	<p>The demand for interventions for enhancing skills and competences and the matching of labour market needs and education/training offerings will be increased.</p> <p>Also the priorities for infrastructural endowment of regions will be affected requiring ICT and accessibility infrastructure allowing for the interconnection of knowledge hubs and the dispersion of economic activities.</p>	<p>Depending on the approach of the Cohesion policy (supporting the weaker, supporting the strong, supporting the strengths etc.) polarisation might continue.</p>	<p>LRA apart from the provision of locations will have to promote partnerships with the business sector and the society and also by attracting stakeholders via the “non-basic” sector.</p>

<u>Institutions</u>	<p>11. <i>Diversifying approaches to governance.</i></p> <p>12. <i>Rise of the individual</i></p> <p>14. <i>Public Debt Dynamics</i></p>	<p>Cohesion Policy addresses institutional capacity and governance (1) directly e.g., through TO11, (2) indirectly (as a side effect of sectoral policies, e.g. in the context of the WFD) and (3) methodologically (through the principles of partnership, subsidiarity, multi-annual planning, evaluation etc.). Overall the demand for Cohesion Policy interventions will rise.</p>	<p>Impacts can be affected either by the long time needed for institutional transition and by the limitations of public debt dependency paths and austerity fixation.</p>	<p>LRA will have to further develop participative models of governance and enhance regional economic and accountability cycles.</p>
<u>Globalisation / External policies / Tackling of increasing geostrategic risks</u>	<p>6. <i>Increasingly multipolar world</i></p> <p>7. <i>Intensified global competition for resources</i></p> <p>15. <i>Tensions on the energy market</i></p>	<p>Through the globalisation trends insecurity and volatility will increase. For cohesion policy interventions the focus lies on resource efficiency and energy security. Overall the demand for Cohesion Policy interventions will rise.</p>	<p>Global players might outbid the EU in the race for resources. Also the lack of a mechanism for securing geostrategic interests of the EU as such could render the impact of Cohesion Policy marginal.</p>	<p>LRA will have to strengthen the resilience of their regions in relation to global “shocks”.</p>

This table offers an abstract and simplified picture of the reality; in many cases global trends are positive drivers for Cohesion Policy instruments; however there are cases where global trends dwarf Cohesion Policy interventions or surpass them.

For LRAs the focus is clearly on softer instruments of incentives provision and information & organisation rather than the “classical” regulative policy tools.



### **3 Effectiveness, Efficiency and Governance of Cohesion Policy at regional and local level**

Cohesion policy is the only effective political device that forces different levels of government to cooperate. Therefore, not only good working institutions but also representative institutions taking into account opinions and interests of all actors involved are important for the future development of the regions.

Efficiency and effectiveness of public administrations at national, regional and local levels have a significant impact on economic development and job creation, and thus on increasing social, economic and territorial cohesion.

Likewise, the role of different actors in delivering Cohesion policy objectives as well as the modes of decision-making and public participation influence results and impact in social, economic and territorial cohesion.

Key questions to be tackled in this section are:

- mechanisms to ensure respectively to improve policy delivery across all stages of the programming / project / policy cycle,
- options for CoR to provide an impetus to discussion and to strengthen the role of LRAs

Differences between decentralised countries like Germany or Austria and countries with rather centralised systems such as Czech Republic and Poland which have introduced integrated Regional Operational Programmes in the period 2007-2013<sup>115</sup> will be analysed.

#### **3.1 Analysis of the policy cycle and the different approaches**

As much as Cohesion Policy cannot be captured and contained in the debate of one or two key policy dimensions, also the different stages of the policy implementation must be considered separately. In our view it is important to focus on all elements of policy delivery in order to contribute to a comprehensive debate. The chosen approach supports a diverse debate but at the same time safeguards that crucial points are not being neglected.

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<sup>115</sup> Albeit with a comparatively small financial weight compared to the sectoral programmes.

The guiding structure of the analysis will therefore be the stages of the policy implementation in Cohesion Policy.

It is important to understand the evolution of Cohesion Policy in order to picture future policy options. A brief review of the major reform steps since 2000 as well as an assessment of their actual impacts is therefore presented in table 11.

**Table 18. Major reform steps and assessment of their impacts since 2000**

<b>Reform steps for/in 2000-2006</b>	<b>Reform steps in 2007-2013</b>	<b>Key impacts</b>
<b><i>Gradual extension of the scope of the partnership principle:</i></b> involvement of authorities responsible for the environment and for the promotion of gender equality	<b><i>Gradual extension of the scope of the partnership principle:</i></b> involvement of Non-Governmental Organisations (NGOs) and civil society bodies	Multilevel governance (MLG) can, under right conditions, contribute to greater policy effectiveness in all aspects of programme implementation, to greater legitimacy and transparency in decision-making processes and to greater commitment and ownership of programme outputs. The degree of effectiveness usually depends on prior experience of partnership working as well as national institutional, administrative and cultural traditions.
<b><i>Improvements of the legal base for SF:</i></b> Introduction of a new 'general' regulation <sup>116</sup> replacing the coordination regulation, besides five new regulations on the ERDF, ESF, EAGGF, FIFG and CF	<b><i>Simplification:</i></b> introduction of two programming steps instead of three – planning at national level (NSRF) and implementation at OP level A single Commission implementing regulation for the 2007-2013 programming period which has replaced 10 regulations for the 2000-2006 period Cohesion Fund programme management rules have been aligned with those of the Structural Funds.	Greater clarity for programme management bodies and increased options to align implementation principles across the funds  Limited impact on cross-funding at level of projects

<sup>116</sup> Published in Official Journal of the European Communities L 161, 26.6.1999.

<b><i>Provisions for financial control and discipline:</i></b> (1) Introduction of a performance reserve of 4% which was reserved at MS level in the periods' beginning to those programmes which were performing best at the periods' mid point (2) n+2" rule was introduced in order to accelerate the implementation routines (3) Introduction of the system of ex ante mid-term and ex post evaluations	<b><i>Concentration and streamlining:</i></b> (1) a certain share of resources should be earmarked for the key investments linked to the renewed strategy for Growth and Jobs. (2) increased focus on the proportionality principle	Stronger financial control and fostering performance and result orientation Stronger involvement of MS and regions in programme monitoring albeit reporting of outcomes at EU-level remains a challenge due to lack of unified indicator systems in particular in ERDF
<b><i>Cooperation Programmes:</i></b> Cross-border, transnational and interregional cooperation, introduction of INTERACT and URBACT as network programmes	<b><i>Cooperation Programmes:</i></b> ETC as policy objective in CP, introduction of the EGTC as vehicle for cooperation among public actors Growing role of macro-economic strategies – cooperation programmes should act as policy lever	Stronger alignment of programming and management routines with mainstream programmes; slow but steady pick-up of the new option of EGTC
<b><i>Enlargement:</i></b> Agenda '2000' <sup>117</sup> paved the way for the biggest enlargement of the EU: 10 new MS joined in May 2004	<b><i>Enlargement:</i></b> Bulgaria and Romania joined in 2007	20% increase in the EU's population, but only a 5% increase in the Union's GDP; Increased disparities in income and employment
<b><i>European Neighbourhood Policy:</i></b> Instrument for Structural Policies for Pre-Accession (ISPA) and the Special Accession Programme for Agriculture and Rural Development (SAPARD)	<b><i>European Neighbourhood Policy:</i></b> Instrument for Pre-accession Assistance (IPA) replaces ISPA and SAPARD	Governmental and institutional preparation and support of candidate and potential candidate countries to prepare for possible accession with regards to regional development and cooperation
	<b><i>New policy instruments:</i></b> Jaspers, Jeremie and Jessica	Improvement of cooperation between the EC and the EIB; strengthening of capacity-building and ensuring that MS and regions establish a sound and efficient use of funds.

Source: own considerations.

<sup>117</sup> Agenda 2000: For a stronger and wider Union, Communication of the European Commission COM(27) 2000 of 16 July 1997.

The fourth Report on Economic and Social Cohesion together with the Cohesion Forum on 27 and 28 September 2007 marked the launch of the debate on the future of EU Cohesion Policy beyond 2013.

Since the 2007-2013 period the support of Cohesion Policy with the aid of strategic papers and comprehensive guidelines increased which in turn increased the challenge for national level and LRAs to translate it into meaningful interventions as part of a place-based approach. Also EU 2020 strategies and the required translation into national strategies bears the inherent risk of a trade-off between the strategic guidelines at EU and national level and the reality of Cohesion Policy resp. the actual use of Structural Funds.

The following review will focus on the approach of MS in the period 2014-2020 but factual evidence and analysis is only available for the period 2007-2013 and preceding periods. Many reform steps for 2014+ stem from the shortcomings in the period 2007-2013 and – vice versa – any conclusion on the effectiveness and efficiency in the period 2014+ have to rely on the experiences made so far.

For the period 2014-2020 significant efforts to enhance effectiveness and efficiency through the introduction of new elements and mechanisms in policy delivery have been made. These new elements have to be considered as responses to weaknesses and shortcomings which have been observed in the period 2007-2013. A debate on the future of Cohesion Policy should place due emphasis upon such new elements which aim at improved policy delivery.

A summary of major new elements which have been introduced in the policy delivery chain for the period 2014-2020 is presented in table 15.

**Table 19. Summary of new elements in the policy delivery chain in the period 2014-2020**

<b>Step</b>	<b>Key weaknesses</b>	<b>EC responses in the period 2014-2020</b>
<b><i>Policy coordination</i></b>		
Coordination between the Funds at EU level	Lack of clear demarcation lines, untapped synergies (e.g. in rural development), inherent goal conflicts	Common Provisions and Common Strategic Framework (CSF) covering European Regional Development Fund (ERDF), European Social Fund (ESF), European Agricultural Fund for Rural Development (EAFRD) and Cohesion Fund (CF)



Coordination between the Funds at MS level	Same as above	Partnership Agreement (PA) concluded between EC and MS Introduction of instruments such as ITI and CLLD Anchoring also agreement with specific provisions for the treatment of territorial features Designation of body and committee in charge of coordination at MS level
<b>Programming</b>		
Analysis, needs assessment in policy areas clustered along ESIF	Lack of strategic focus in many areas	Introduction of ex ante conditionalities; i.e. the need for MS to develop strategic guidance in key sectors as a pre-condition for Union support
Strategy development	Prevalence of top-down expert planification and rather rarely actual strategy development according to the idea of MLG Lack of consistency	Code of conduct on partnership-building  Already established steps addressing mainly the risk of lacking consistency: <ul style="list-style-type: none"> <li>▪ ex ante evaluation</li> <li>▪ interservice consultation</li> </ul>
Definition of measures	Lack of focus in programmes, Lack of quality approaches and tendency to avoid truly innovative approaches	Definition of Investment Priorities in the Regulation
Allocation of funds	Lack of focus	Rules on thematic concentration: obligatory financial allocation, which gives the thematic concentration a much higher enforcement.
<b>Implementation</b>		
In general	Lack of coordination at programme level, partly lack of accountability National administrative systems encounter difficulties to efficiently integrate key administrative requirements for ESI-Funds thus often leading to disproportionate burdens for programme management and beneficiaries	Shared performance review in 2019

Support of beneficiaries at the application stage	Lack of experienced staff Lack of neutral intermediaries which have the capacities to effectively support the LRAs	Focus on capacity-building with Thematic Objective 11, request for strategic policy framework with regard to administrative efficiency at MS level
Assessment	Lack of experienced staff some measures are de-facto being implemented without any compulsory assessment (SME support)	Ex ante assessment by the Commission in case of financial instruments, also option for revision during implementation
Selection	Lack of experienced persons in the selection committees Moral hazard problem	No additional or specific provisions on this crucial point – in general strengthened responsibility and duties of the MA (management verification)
Contracting	no particular weakness identified	----
Implementation of operations	Significant administrative burdens for beneficiaries Procurement as persistent challenge accounting for significant percentages of the error rate	Specific considerations on reduction of administrative burden requested in Programmes Directive on Procurement COESIF Guidelines for financial corrections in case of infringement of procurement rules
Disbursement	Lagging pace of implementation	Already established: n+2/n+3 rule and automatic decommitment Provisions for non-performing projects related to 07-13 TO dedicated to capacity-building (TO 11) Stronger link between economic performance and ESIF in the PA Provisions for phasing of projects
Financial control	Long periods for control, steadily rising requirements during the funding period (which is rarely subject of inter-institutional knowledge management)	Simplified cost options anchored in Regulations and elaboration of guidance documents, streamlining simplification options such as standard unit costs, flat rates, simplified treatment of revenues or instruments such as the Joint Action Plan (significant effort in development but quite simple in terms of implementation and control)

<b><i>Control of the delivery system</i></b>		
Evaluation and control	Lack of goal and result orientation	Result and performance indicators, compulsory and comprehensive performance review in 2019 Evaluation compulsory again, need for evaluation plans at programme or MS level
Audit	Various shortcomings in the control system but also in the audit system (in the latter case detected by the Commission) – in part strong focus on formal aspects in audit	New elements in CPR: emphasis on anti-corruption and anti-fraud measures where MS are now explicitly required to present risk assessments and adequate instruments (e.g. Arachne)

*Source: own considerations.*

The policy stages used in the table also structure the following review on the efficiency and governance in Cohesion Policy.

## **Policy coordination at EU level**

Theoretically, cohesion policy for 2014-2020 is in line with the EU's overall economic policy coordination which is monitored through the European semester process. To ensure better coordination and less overlaps, within the new programming period the Common Strategic Framework (CSF)<sup>118</sup> provides the basis for better coordination between the ESI Funds. It provides links to other EU instruments such as Horizon 2020 and the Connecting Europe Facility.

The CSF is broader, better justified and more coherent than the Community strategic Guidelines for 2007-2013. It has been welcomed as a useful asset and is expected to bring more coherence and coordination to the planning and implementation of ESI Funds. However, according to some Managing Authorities it does not go far enough given that there are still separate Fund-specific regulations (especially for EAFRD). The need to go further on integration of the ESI Funds and coordination between the Commission Directorates-General is obvious.<sup>119</sup>

As a result of new goals added in each period the risk of goal conflicts has increased. The risk of efficiency losses due to inherent discrepancies between goals tends to be neglected.

Main examples of conflicts between goals exist at different scales:

<sup>118</sup> The Common Strategic Framework is an annex to the umbrella Common Provisions Regulation (CPR) that covers five Funds in different policy areas.

<sup>119</sup> EPRC 2015, Strategic coherence of Cohesion Policy: comparison of the 2007-13 and 2014-20 programming periods.

- at large scale: conflict between an approach driven by the focus on competitive technologies and centres of excellence versus the reduction of disparities or support to employment in agriculture versus support to restructuring and diversification;
- at small scale: conflict between cost-efficient solutions and sustainable low-carbon solutions in public transport (requirements in Investment Priority 7C) against the background of shrinking public investment capital in particular for LRAs in challenged regions;
- The communication between the MS and the European Commission was based on different channels<sup>120</sup>:
  - the draft legislative packages published in autumn 2011 as well as the draft delegated and implementing acts and informally distributed documents presenting the changes agreed during trilogies,
  - the guidance material and the EC Position Papers,
  - Information flows via the relevant committees and direct communication with respective EC desk officers.

Implementing a balance between the overall economic policy coordination at EU level and meeting specific needs of the territories led to national challenges as described in the PAs. During the policy coordination process it was specifically challenging to overcome the gap between the Country Specific Recommendation and national strategic and programme documents. A more collaborative approach between the European Commission and Member States in developing both the Common Strategic Framework and the Position Papers should be considered. Moreover, the application of the partnership principle could be monitored by the European Parliament.<sup>121</sup>

Also, the legislative package was interpreted differently by different MS. The debate about indicators was especially ambiguous between different stakeholders and the verbal communication between MAs and desk officers was sometimes misunderstood in comparison to written comments (*ibid.*).

Nevertheless, a review of the adopted PAs<sup>122</sup> showed that no major hurdles appeared when establishing coherence between national needs as defined in national development programmes and the Country Specific Recommendation and National Reform Programmes (NRP) and the requirements of thematic concentration and the Europe 2020 targets.

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<sup>120</sup> Metis, 2014, Implementation of Cohesion Policy 2014-2020: Preparation and administrative capacity of Member States, European Parliament Policy Department B: structural and cohesion policies.

<sup>121</sup> ERCR 2015.

<sup>122</sup> Metis, 2015a, Study on “Review of the adopted Partnership Agreements”, in progress.

Coordination and synergies between the ESI Funds and other Union and national funding instruments and the EIB is organized in dependence of the country size. For instance, in smaller countries, one ministry can be responsible for a range of European programmes.

The PAs and OPs have a key role in strengthening the consistency and integrity between the funds, as well as between the EU strategies and policies and the national strategies and policies in terms of<sup>123</sup>:

- establishing links to economic strategies at EU level (Europe 2020) as required in the Common Provisions,
- creating and manage coherence with national strategies and policies,
- securing better coordination with funds.

### **Policy coordination at Member State level**

The 2014-2020 programming period is also characterized by closer cooperation between different partners in MS. Regional and local partners (including urban partners, social and economic partners, and civil society) were involved in the preparation of the PA concluded between the Commission and each MS as well as the OPs.

Policy coordination is one of the overarching systematic challenges for effective public investment. Challenges for MLG coordination refer to cross-sectorial, cross-jurisdictional and intergovernmental coordination.<sup>124</sup>

The challenging types of policy coordination are vertical coordination and horizontal coordination. Vertical coordination, i.e. from central level to LRAs mostly implies difficulties in centralised MS where sub-national levels frequently lack information on central government priorities and vice versa. Moreover, administrative and regulatory obstacles hinder efficient coordination.

Horizontal coordination is probably even more challenging since it should cross the boundaries between established players in the political-administrative system. The challenge at all tiers of government is also reflected in cohesion policy: Despite all efforts of the Commission to establish incentives for cross-fund investments, these have remained rather the exception in the period 2007-2013.

Various mechanisms exist to strengthen vertical coordination across levels of government<sup>125</sup>, such as national investment strategies, territorial representatives,

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<sup>123</sup> Metis, 2014.

<sup>124</sup> OECD 2014, Recommendations of the Council on Effective Public Investment Across Levels of Government, adopted in March 2014, p. 6.

regional development agencies and formal agreements. Within cohesion policy coordination processes can be improved due to the principle of co-financing, formalised consultation processes, dialogue platforms as well as informal coordination arrangements.

According to the OECD<sup>126</sup> in federal or quasi-federal countries either cross-regional or cross-local collaboration exist which is not the case in some traditionally centralised countries (except FI and FR), which put less emphasis on horizontal collaboration.

## **Different implementation systems**

Comparing implementation systems between national and regional policies and European policies different institutional backgrounds lead to a broad diversity of approaches. Cohesion Policy is dealing with domestic and EU-funds and is always delivered through national or regional systems. In countries where EU Cohesion Policy accounts for the overwhelming share of funds, the principles of the EU-intervention logic rule the implementation. The difference between countries is in particular relevant for EU15 and EU12/13 countries<sup>127</sup>:

In EU 12/13 – with high shares of Cohesion Funds – the reform of the public sector since the early 90ies poses multiple challenges such as the re-establishment of local self-governance, the rapid and parallel evolution of the information and the civic society and – with regards to Cohesion Policy – the rapid transformation of the economy which happened at a much quicker pace than the change of political realities. Subsequently some countries started the process of administrative decentralisation and hence, the whole public sector had to undergo a profound reorganisation. The main challenges in the case of EU12 (without CY and MT) are:

- the dominant principle of hierarchy, and the need to deal with non-hierarchical working methods as the cross-sector coordination requires – usually the Ministries or authorities in charge of coordination have very limited options to achieve coordination of implementation,
- a partial lack of experience and knowledge base in the public administration due to staff fluctuation – and as one reaction a quite rigid approach to formal aspects: in worst case the assessment of formal aspects outweighs the assessment of contents of operations,

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<sup>125</sup> OECD 2007, Linking Regions and Central Governments: Contracts for Regional Development, OECD Publishing, doi: 10.1797/9789264008755-en.

<sup>126</sup> OECD 2013, Investing Together. Working Effectively across Levels of Government, p. 72.

<sup>127</sup> Metis 2011, The complementarity of national and Community interventions aimed at reducing disparities in economic and social development, Commissioned by Committee of the Regions, DTC Unit 4.

- the inherent risk that project generation capacities dominates over actual priorities and needs; this is paired with the challenge for LRAs to provide the required own contributions – LRAs most in need of support might fall short to succeed in acquiring projects,
- the need to improve transparency and accountability.

In EU15 a much longer period of mutual adaptation of domestic and Cohesion Policy has taken place. With EU funds being much less significant in terms of public expenditures a variety of approaches – ranging from complete integration of Cohesion policy in domestic delivery systems (AT, DE) up to the establishment of separate structures - have been developed. During this period new and interesting approaches seem to concentrate in the northern MS (DK, FI, SE). Some of the challenges in EU15 are similar to those in EU12 some are different:

- Established structures tend to be reluctant to change: it seems that integrating EU funds completely into domestic structures creates difficulties in the way as domestic systems need some alignment to comply with Cohesion policy rules.
- Without political entrepreneurs fuelling the process - i.e. developing new approaches to policy monitoring, reporting and cross-sector negotiation procedures – coordination will remain at a strategic level without having major impetus on policy delivery; sophisticated and fragmented structures and broad numbers of involved actors tend to make the adjustment of the agenda more demanding.
- Visibility of EU Cohesion Policy is a challenge – it tends to have its major influence in improved strategic coordination but not in policy delivery.

## **Coordination mechanism**

In most EU countries (24), the coordination of the ESIF is in the hands of the sectoral ministries and coordinated through an inter-ministerial committee or in the hands of a government body<sup>128</sup>.

The coordination of funds is often supported by the Monitoring Committees. Therefore, the Monitoring Committees of the various OPs often serve as coordination mechanism due to cross-representation, i.e. Members of different Committees attend each others' meetings or are responsible for more than one

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<sup>128</sup> Metis 2015a.

fund (BG, EE, GR, FI, HU, IE, IT, LV). Moreover, a number of countries have established thematic networks or working groups but also websites on specific policy fields, sometimes across funds. Contact persons per MA that have knowledge of other funds at EU and national level are appointed and the involvement of other programmes as Erasmus+, Horizon 2020, Life+ and ETC programmes is guaranteed (*Metis 2014*).

One major problem however is the tradeoff between the coordination which is anchored at MS level – mostly as a consequence of provisions in the PA – and the needed coordination between the operative management of the programmes:

- ESIF coordination committees will in most cases not refer to the level of operations but discuss rather strategic issues and guidelines to support (and accelerate) the pace of implementation.
- Options and communication routines for a regular exchange between the operative units involved in programme management rarely exist – thus in practice e.g. firstly an operational definition of demarcation lines between programmes is often lacking thus increasing the risk of uncoordinated or parallel actions or secondly, operational policy levers for investment coordination might not exist.

Strengthening collaboration where it has historically been weak involves certain risks because of a lack of or limited inter-institutional trust on the sub-national level. According to the OECD (2013) this stems from a planning tradition (such as in PL) that orients localities vertically, towards the centre.

For the period 2014-2020 the introduction of instruments such as integrated territorial investments (ITI) and community-led local development (CLLD) shall meet coordination as well as territorial challenges in the EU. The place-specific approaches might go beyond administrative boundaries and therefore requires great willingness from different government levels, meaning vertical and horizontal coordination. As a result, a stronger focus on the territorial impact of EU policies combining investments from several priority axes of one or more OPs for the purposes of multi-dimensional and cross-sectoral intervention are expected.

CLLDs are used in all 28 MS, ITIs in 20 MS. Austria, Belgium (Walloon), Germany, Malta and the Netherlands include CLLD as a continuation of the LAGs under the EAFRD. Other countries combine ERDF, EAFRD and EMFF (Cyprus) or EAFRD and ESF (Germany – Saxony-Anhalt) or EAFRD and



EMFF (Denmark) or EAFRD, ERDF and ESF (Spain), all four funds (Sweden) in an integrated CLLD approach or use a mono-fund CLLD-approach<sup>129</sup>.

Most countries address the urban dimension (22), mostly under ITIs. Often, ITIs are used exclusively for the urban dimension, e.g. in Croatia and Slovenia. Bulgaria even provides – in line with the National Spatial Development Concept for 2013-2025 – considerable support from ESIF for integrated actions for sustainable urban development in the 2014-2020 period in order to tackle the economic, environmental, climate, demographic and social challenges in urban areas (*ibid.*).

Most countries are involved in macro-regional strategies and sea basin strategies supporting ‘blue growth’. The EU Strategy for the Danube Region (EUSDR) and the EU Strategy for the Baltic Sea Region (EUBSR) have an important place in the Partnership Agreements of the countries involved mentioning possible synergies with and distinction of measures in the ESIF OPs.

In view of the foregoing, regions and places are increasingly considered as the key level for establishing more efficient policy coordination. The same can be concluded for the next policy stages – from the design to the implementation phase. At the same time it must be stressed that an effective and efficient implementation of these new instruments requires new coordination mechanisms to ensure timely project elaboration and adequate implementing provisions which support cross-funds approaches.

## **Programming**

The general environment in which MS’ authorities prepared the 2014-2020 programming period was characterized by the continuing impacts of the financial crisis and political and institutional changes. MS that were particularly vulnerable in the crisis tend to use ESI Funds to compensate for budget cuts at national and regional levels instead of reflecting the long-term effort to create sustainable and socially equitable development.

However, the thematic concentration of cohesion policy instruments along 11 Thematic Objectives helped to steer ESI Funds to meet specific pre-determined purposes. To bring funding in line with Europe 2020, the ERDF is targeted in particular at the first four key priorities such as innovation and research, information and communications technologies; small and medium-sized enterprises (SMEs); and the transition to a low-carbon economy. In less developed regions, greater flexibility was granted. Nevertheless, the thematic concentration on these priorities was seen critical in MS where a strong focus on

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<sup>129</sup> Metis, 2015a.

infrastructure and tourism support dominated the 2007-2013 programming period<sup>130</sup>, i.e. EU12 MS. In countries with previous experience in ERDF OPs that focused on support for SMEs and innovation and research had less difficulty adjusting to the intensified thematic focus, i.e. most of the EU15 MS (*ibid.*).

In most countries the development needs correspond more or less to the objectives of ESI Funds. However, some countries have particular approaches either on account of economic or territorial specificities<sup>131</sup>:

- Because of the particular position of Greece an only “growth approach” based on TO1, 2 and 3 would not be beneficial. Therefore it was decided to “address all Thematic Objective based on the acute needs due to the economic crisis, the Recommendations of the Council, the requirements of the Stability Pact and the Economic Adjustment Programme.
- In France – where decentralization resulting from the policy changes in the 2014-2020 period has a positive impact on the future bottom-up policy making in Cohesion Policy – the PA highlights the need for a territorial approach due to the differences across the country. Here, the PA “serves as an instrument to create a coherent approach towards reducing the challenges between the European, the national, the regional and the local levels (PA France).
- Disparities, development needs and growth potentials at TO level as well as territorial challenges differ in Italy. Hence, a distinction between inner areas, urban areas, and rural areas was implemented.
- Slovakia concentrates the TOs and priority areas of support into individual geographical territorial units stipulated in the national Concept of the Territorial Development of Slovakia planning document. The PA aims to ensure the implementation of investment priorities in those areas which have the highest development potential for the given priority.
- The Netherlands and Luxembourg that do not face such territorial differences resp. have a very small territory presenting a strong alignment between the thematic concentration, country performance on EU 2020 indicators, Country Specific Recommendation and development needs.

For the ESF, the regulation foresees during the 2014-2020 programming period that ‘at least 20% of the total ESF resources in each MS shall be allocated to the Thematic Objective 9 “promoting social inclusion, combating poverty and any discrimination”’.

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<sup>130</sup> Metis, 2014.

<sup>131</sup> Metis, 2015a.

In addition, the regulations provide for multi-fund programming from 2014-2020 enhancing general policy coordination. This was very well received by the MS, as 92 out of 216 OPs are multi-fund programmes including ERDF and ESF funding. Eight MS (AT, BE, DK, IE, LU, NL, ES and the UK) did not implement multi-funded OPs, mostly because of their sectoral approach with different Ministries being responsible for the different ESIFs and implementation. Likewise, in MS with very coordinated approach to the PA such as Austria, the logic of mono-funded OPs prevailed (*ibid.*). Besides, the overall number of OPs has been reduced due to the reduced amount of funding and the high administrative overheads related to managing each OP.

Fund-specific regulations provide for a translation of thematic objective into an exhaustive list of “investment priorities” which can be also seen as objectives leaving flexibility to design the optimal mix of actions.

Article 5 of the Common Provisions Regulation (CPR) provided the legal basis for adoption of a delegated act on a European Code of Conduct on Partnership (ECCP). It should help MS in organizing a meaningful partnership with relevant stakeholders. Experience shows diverse interests of different stakeholders, complexity of decision-making and demanding intervention by the European Commission.

In all PAs, the NRP translate EU objectives into national targets and present MS’ policies and measures to sustain growth and jobs and to reach the Europe 2020 targets. The review of adopted PAs discovered that Country Specific Recommendations are sometimes even broader in reach than the priorities of the ESI Funds. Both, the Country Specific Recommendations and the NRPs were found to be consistent with respective national strategies. Moreover, relevant parts were decisive for the choice of TOs and priorities in the OPs.

Prior the approval of the OPs, interservice consultations between different Directorate Generals of the Commission were obligatory. In addition, ex ante evaluations were undertaken for each OP which proved to be very supportive in improving the Partnership Agreement process.

A Metis study<sup>132</sup> on the implementation of cohesion policy comes to the conclusion that the “process of developing the PAs was one of ‘multi-level governance’, given that it was based on the involvement of a large number of different partners. All of the MS analysed in the case studies<sup>133</sup> had established platforms, working groups, PA committees, thematic working groups, and public consultations”.

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<sup>132</sup> Metis, 2014

<sup>133</sup> The selection of case studies encompassed OP changes, the size of the Structural Funds budget, and individual Member State characteristics: Austria, Finland, Luxembourg, Sweden, Estonia, Croatia and Bulgaria.

On the other hand, “this resulted in higher expectations of having influence on the PA and OP development or receiving a larger share of the EU Funds, which are seen as an important financial source in a context of public finance shortage”. In such cases, the Commission had to adhere very strictly to the TOs recommended in the Position Papers published in 2012.

Moreover, different elements of the programming process and the adjustment of PAs and OPs lacked efficient coordination (*ibid.*):

- MS sometimes started too early with the preparation of the Partnership Agreements and the Operational Programmes and had to adjust the structure and content to meet the changing guidance materials. In some cases, this was due to a lack of understanding about the significance of the Position Papers.
- Regional and national analyses had been elaborated in parallel by regional and national authorities. The MAs of the OPs were only scarcely involved at the beginning of the PA development. Therefore the input for the PA which should serve as an umbrella document for all ESI Funds OPs was sometimes insufficient which made readjustments necessary.
- The involvement of numerous partners in the PA development resulted in complex and lengthy discussions that made the achievement of consensus difficult.
- MS characterized by a strong regional political system had difficulties in effectively coordinating the development process for the PA and OP.
- Communication with the European Commission was seen as difficult, because different units of the European Commission assessed the Partnership Agreements and Operational Programmes differently.
- In some cases, the recommendations of the ex ante evaluation contradicted the recommendations of the EC, which created confusion among the MA and public authorities.
- The inclusion of the EAFRD and EMFF in the 2014-2020 periods’ PA were in some countries considered as advantage (Greece) and in some as challenging (Germany).
- Effects of the economic crisis and related austerity measures (particularly in Convergence regions, presented by the example of Italy) resulted in considerable effort to limit the damage of possible loss of resources and accelerated the progression of expenditure. Implemented measures – even

if they paid off – distracted human resources and time from the task of programming the 2014-2020 period.

- In some countries, the partnership process led to institutional reforms and changed mindsets in the OP structure.

Answering the need to improve the quality of public expenditure as emphasized in the 2010 Budget Review conditionality provisions were introduced into cohesion policy 2014-2020. Ex ante conditionalities therefore support the development of strategic guidance in key sectors as a pre-condition for Union support. They are divided into general conditionalities applying to all ESI Funds and thematic conditionalities applying to specific funds. Fulfilment of ex ante conditionalities is presented in the PAs as well as in the OPs. In case of non fulfilment, an action plan must be provided in close cooperation between the MS and the Commission.

Ex ante conditionalities support the strategic foundation of interventions. However, some MS perceived the clear guidance and assessment practice of the Commission as interference in national policy practice. Intense coordination and negotiations between the Commission and MS led the way to a common decision. The process was often considered as challenging, but some MS recognized the provision of new perspectives for various sector-oriented government levels (*ibid.*).

First results of an ongoing study of the state of implementation, differences and similarities between MS, PAs, OPs and different ESI Funds<sup>134</sup> reveal considerable social, economic and territorial disparities<sup>135</sup>:

- MS with a dominant share of more developed regions are clearly ahead in fulfilling the ex ante conditionalities. In other words, the majority of ex ante conditionalities in EU12 are still in the process of implementation.
- The fulfilment rate of the General ex ante conditionality “existence of arrangements for the effective application of Union State aid rules in the fields of the ESI Funds” is the highest. However, fulfilment rates vary according to types of regions revealing higher degree of fulfilment in more developed regions compared to less developed regions and mixed regions including outermost regions. The highest level of fulfilment is

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<sup>134</sup> Metis 2015b, The implementation of the provisions in relation to the ex-ante conditionalities during the programming phase of the European Structural and Investment Funds, Interim Report in progress.

<sup>135</sup> In the first phase of the PA and OP screening all PAs and 174 OPs out of 216 have been screened. OPs belonging to more developed regions represent the highest amount of screened OPs at the current time (May 2015).

shown by the adjustment of environmental legislation, the lowest can be seen for the statistical system.

- The majority of MS have addressed the requirements stemming from the conditionalities in a participatory process involving diverse stakeholders combined with capacity building and cooperation between different public organizations. Actions to be undertaken refer to a broad range of actions such as e.g. the nomination of authorized persons dealing with anti-discrimination or gender equality or the training and capacity-building for state aid experts.

The European code of conduct was provided in order to support and facilitate MS in the organisation of partnerships for Partnership Agreements and programmes supported by the ESI Funds<sup>136</sup>. Usually, there is a quiet visible investment at the start of the programming process. However, when it comes to a needs assessment and the definition of cornerstones of the investment strategy negotiations with the Commission often result in amendments to the strategic orientation. During this stage, socio-economic partners are less involved.

## **Implementation**

Programme management and implementation systems must comply with EU Cohesion Policy requirements. Nevertheless, the institutional and administrative contexts of different MS require a certain flexibility to adapt Programme implementation to the political-administrative system of the MS. As a result, variations in the management structures, the number of actors involved and the delegation of tasks to intermediate bodies across the programmes exist across the MS. Moreover, the scale and thematic content of programmes has a massive impact on the number and types of actors involved.

Countries with more centralised government structures tend to have more centralised systems for managing Cohesion Policy than federal countries. However, previous research indicates that this relationship does not fully hold because there are highly devolved countries which grant a stronger role for national ministries (as in Spain) or vice versa (as in England)<sup>137</sup>.

Key bodies in OP management and implementation are the MA and the related control bodies for the verification of expenditures, Certification Authority and Audit Authority. In general, the MAs are integrated into government Ministries or agencies at national or regional level. The Certification and Audit Authorities are responsible for certifying/paying funds to beneficiaries and auditing systems

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<sup>136</sup> Regulation No 240/2014.

<sup>137</sup> Metis, EPRC 2013, An assessment of multilevel governance in Cohesion Policy 2007-2013.

and expenditure respectively. In the majority of MS these tasks are covered by different sections of the Ministries of Finance.

Looking at the past period 2007-2013 the extent of MLG differs across different management tasks: bodies with responsibility for financial compliance and payments tend to be more centralised than bodies with responsibility for the general management and coordination of substantive policy content issues and project selection (*ibid.*).

### **Assessment of projects**

In general, the assessment of projects prior to approval is one of the essential steps to ensure a high quality of project outcomes. At first we would like to concentrate on assessment in case of infrastructure related OPs which address the local or regional level. In particular when it comes to such programmes in EU12/13 there are several important challenges linked to the assessment:

- In programmes with a broad focus such as in integrated Regional OPs (ROPs), a consistent assessment of constant quality is harder to achieve than in programmes with a narrow focus and rather standardised project designs.
- Due to the high number of incoming projects as part of call cycles the time frame for assessors is often quite short and does not allow for proper calibration and thorough discussion of individual assessments.
- Key aspects of cost-efficiency, cost benchmarks and other types of solid guidance are often lacking and thus resulting statements are quite vague.

In such programmes – e.g. in ROPs or OPs on smaller-scale environmental infrastructure – the basic requirements for transparent selection are comprehensive. A fair selection procedure requires comparable information on all projects or bundles of projects respectively measures as well as a culture of open debate in the selection committee(s). For obvious reasons, the quality management in assessment and selection falls mainly in the responsibility of the MA, i.e. mainly ensuring the quality of information for decision-making and safeguarding an open climate in the debate.

The situation might differ in countries with a decentralised administrative structure and a tradition of programmes in regional policies (such as e.g. in AT, DE, FR) where the process of project development might even be a corporate venture between local and regional level. In such a context project maturity and coordination prior to project submission become decisive arguments to place a project in a certain programme. Here, the assessment and selection in the

programme marks rather the end of a shared development process than an actual decision.

Again a different case is project selection in fields of SME-support or in case of financing instruments since here decisive parts of the assessment routines are in hands of Intermediaries (such as funding agencies or even banks) and the decision on selection follows guidelines and principles.

In general great challenges of ex ante appraisal are most likely where there is considerable uncertainty about the factors affecting returns on investments<sup>138</sup>. The different types of risks and uncertainties which are associated with public investment, including long-term impacts, should be duly assessed at an early stage of the investment cycle as part of the appraisal. Such risks might include fiscal risks (e.g. contingent liabilities) as well as political, social, and environmental risks.<sup>139</sup>

## Project Selection

Project selection is not formally regulated by the partnership principle and therefore falls under the responsibility of the MS. Nevertheless, project selection criteria have to be approved by the Monitoring Committees and therefore key partners such as authorities responsible for the environment and for the promoting of gender equality, NGOs and Civil Society Organisations (CSOs) should be involved. Despite this formal requirement, OP partnership members – especially non-state actors – often have limited influence on the project selection criteria and are not collectively involved in the selection of projects in most of the cases (*ibid.*). Moreover, representatives of CSOs or institutions dealing with horizontal issues often have a marginalised role in the selection committee due to a lack of structured information in order to effectively monitor and comment the process.

The literature shows that MLG in policy implementation can contribute to greater policy effectiveness, greater commitment and ownership in decision making, as well as greater commitment and ownership of programme outputs. These positive effects however depend on prior experience of partnership working as well as national institutional, administrative and cultural traditions. Main challenges related to MLG in programme management have been identified as follows: diffusing or separating management responsibilities, coordination challenges linked to administrative burden, lack of clear guidance and shifts of responsibility. Effective MLG in management and implementation can be facilitated by regular information exchange and targeted training measures (*ibid.*).

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<sup>138</sup> OECD 2014, p. 17.

<sup>139</sup> Cf. OECD 2014, p. 10.



A frequently raised issue which is often related solely to project selection is the so-called moral hazard problem. In Cohesion Policy it refers to the risk that projects with low or no added value are being implemented as part of ESI Funds programmes.

Firstly, it is important to see that the moral hazard problem might stem from different stages of the policy respectively programme cycle as indicated in table 16. Secondly it is important to see that – provided there is a willingness to seriously approach the problem – actions to contain the risk can be introduced in the programme management cycle.

**Table 20. Considerations on the moral hazard problem**

<b>Stage of the programme cycle</b>	<b>Key risks respectively dimensions of the moral hazard problem</b>	<b>Risk prevention / containment</b>
Project development	<ul style="list-style-type: none"> <li>▪ Planning in terms of cost-efficiency (e.g. choice of technology, design of infrastructure)</li> </ul>	<ul style="list-style-type: none"> <li>▪ expert advice, cost-benefit analysis, ex-ante appraisal</li> </ul>
Assessment prior to selection	<ul style="list-style-type: none"> <li>▪ lack of expertise of staff thus risk of low efficiency and effectiveness in particular when it comes to the crucial point of cost-efficiency</li> </ul>	<ul style="list-style-type: none"> <li>▪ capacity-development and option to consult external experts on specific questions</li> <li>▪ cost benchmarks for frequent types of projects</li> <li>▪ guidance for risk assessment according to types of projects</li> </ul>
Selection	<ul style="list-style-type: none"> <li>▪ Conflicts of interest</li> <li>▪ Short-term versus longer-term interests</li> </ul>	<ul style="list-style-type: none"> <li>▪ MA ensuring transparent handling of conflicts of interest in the selection committee</li> <li>▪ Obvious and transparent link between assessment result and selection criteria</li> <li>▪ Tangible selection criteria which are an inherent element of the debate in the selection committee and encourage the selection of projects with sustainable impact</li> </ul>
Project implementation	<ul style="list-style-type: none"> <li>▪ Procurement in terms of cost-efficiency</li> <li>▪ Low quality of outputs and low sustainability</li> </ul>	<ul style="list-style-type: none"> <li>▪ Building-up expertise in the programme management</li> <li>▪ Active support to beneficiaries</li> <li>▪ Highlighting risks related to infringements of procurement law in all guidance documents</li> <li>▪ Establish independent quality control as integrated element of large projects</li> </ul>

Evaluation and monitoring	<ul style="list-style-type: none"> <li>Indicators and the culture of reporting programme outcomes tend to have a rather narrow focus and are hardly useful to capture the risks discussed in the preceding steps of the policy cycle</li> </ul>	<ul style="list-style-type: none"> <li>Re-definition and broadening the scope of monitoring and evaluation</li> </ul>
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*Source: own considerations, OECD 2014.*

## Financial control of operations

One of the key challenges in the implementation of ESIF is the financial control of the operations (also referred to as verification of expenditures). De facto it has been one of the most demanding tasks for most MS to set-up effective and efficient control bodies which are in charge of the control task. National requirements are combined with requirements according to EU Regulations and form the national (or in some cases regional) eligibility rules which guide the work of the control bodies.

Most studies referring to the administrative burden for beneficiaries in fact refer to the requirements inherent to the verification of expenditures. In the period 2007-13 a limit of three months has been introduced but de-facto time spans from submission of payment requests to closure of control routines are often much longer - frequently owed to staff constraints and to lengthy and inefficient communication between control bodies and beneficiaries. The following table seeks to highlight the most important aspects related to this crucial step in programme and project implementation.

**Table 21. Challenges related to verification of expenditures in ESIF**

Key aspects	Challenges
<b>Organisation</b>	
Position in the administrative system	<ul style="list-style-type: none"> <li>Should be independent but is often part of the institution acting as MA or Intermediate Body</li> <li>In case of several bodies involved for the same Funds (e.g. in larger ROP co-funded from ERDF) risk of differing standards</li> </ul>
Staffing	<ul style="list-style-type: none"> <li>These bodies encounter staff constraints and fluctuation of staff more often than other bodies involved in management of ESIF – this might be due to high requirements, high peak work load close to the end of the year (n+2), frustration due to role in the clean-up at the end of pipe</li> </ul>

<i>Tasks</i>	
Development of eligibility rules	<ul style="list-style-type: none"> <li>▪ Should be rather a dialogue between practitioners from the programme (MA, control bodies, AA) in order to have concise and transparent rules but is often done top-down leading to questions of interpretation and other queries</li> </ul>
Definition of the evidence requested from the beneficiary	<ul style="list-style-type: none"> <li>▪ This is the crucial point with most inherent potentialities for the reduction of the administrative burdens for beneficiaries; also e-cohesion will only have limited impact as potential remedy if these requirements are strictly defined by the MS</li> </ul>
Communication with beneficiaries	<ul style="list-style-type: none"> <li>▪ Often the ones to communicate the administrative requirements to beneficiaries and to run lengthy communication loops end-of-pipe due to lack of communication in preceding steps of the project management cycle</li> </ul>
Verification of expenditures and monitoring of outcomes	<ul style="list-style-type: none"> <li>▪ Check of formal compliance, correctness of expenditures and quality of outputs is a task which cannot be met by just one person but requires often cooperation across department (e.g. thinking of larger infrastructures with the need to control procurement procedures)</li> </ul>
Data transfer, storage and archiving	<ul style="list-style-type: none"> <li>▪ Need to transfer correct data to the monitoring system of programmes, transparent records on all control activities, adequate archiving routines pose a considerable challenge in case of large programmes</li> </ul>

*Source: own considerations.*

The set of regulations for the period 2014-2020 has introduced many approaches to simplify the verification process such as standard unit costs, lump sums and flat rates. It is now up to the MS to take up these options and integrate it to the national eligibility rules. Since about one year considerable energy has been spent by most programme managements in MS to develop a new set of eligibility rules – this is particularly challenging for the ERDF with its broad portfolio and differing character and size of projects.<sup>140</sup> A set of guidance documents which was discussed in the Coordination Committee for the ESIF (COESIF) and came out at the start of 2014<sup>141</sup> documents the efforts invested and the vital role of the eligibility rules for the implementation of ESIF. The process of elaborating and discussing the eligibility rules is often impaired by the fact that sensitive points should be clarified ex-ante with the Audit Authority – these feedback loops are often quite lengthy. EC staff has started to step in order to support the clarification process related to simplified cost options. But still the quick and open dissemination to practitioners in MAs and Financial

<sup>140</sup> Ranging from micro-project funds in ETC to revenue-generating projects such as incubator centres.

<sup>141</sup> Such as e.g. the guidance on simplified cost options (SCOs).

Control Bodies must be ensured in order to prepare the control system for the new period.

## **Public procurement**

Procurement ranks among the key challenges for the majority of projects where public entities are involved as beneficiaries or other entities have to apply it due to the high support rates from ESIF. It has been a recurring challenge throughout all funding periods so far. In general, infringements of procurement laws account for 1,005 out of 7,062 reported irregularities in 2010 (14% of cases) and as such it ranks second among the top ten of frequent types of irregularities. With regards to the financial amounts involved, infringement of public procurement rules accounts for almost 17%<sup>142</sup>. However, it is important to note that an error not necessarily insinuates fraud – fraud is intentional.

OECD research indicates that procurement is integral to public investments but it is also the government activity most vulnerable to waste, fraud and corruption. On average, 55% of public procurement spending occurs at the sub-national level. Sufficient capacity building at the sub-national level is therefore crucial.<sup>143</sup>

Nevertheless, procurement has to be understood as a key policy lever: Cohesion Policy accounts for major shares in public investment and it might be used to pursue important strategic or cross-cutting policy objectives such as environment sustainability through green procurement and life-cycle cost models or for example SME development.

The European Parliament and the Council have adopted two public procurement directives in 2004 in order to consolidate procurement procedures at European level. These directives regulate procurement procedures for contract agreements following a unified system of thresholds and procedural requirements depending on the estimated net volume of the services, goods or works. Keeping in mind the high amount of infringements of procurement, Cohesion Policy cannot be subject to any derogation from the public procurement directive at European level. All major arguments in favour of procurement apply the more so in case of Cohesion Policy. However, simplification of the complex legislation would be welcome and the discussion of EU procurement directive should be used to raise awareness that a significant part of the current complexity of Public Procurement is due to the intricacies of national legislation<sup>144</sup>.

Key challenges for LRAs occur in particular at the local level due to shortage respectively lack of experienced staff. In many MS the public procurement

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<sup>142</sup> Metis 2012, Public procurement and Cohesion Policy.

<sup>143</sup> OECD 2014, p. 22.

<sup>144</sup> Metis 2012.

agencies or authorities which should in principle also provide advice to other public bodies are overburdened and cannot offer advice in the short-term. Therefore publicly available guidance is often missing.

## **Control of the delivery system**

### *Monitoring and reporting*

The 2014-2020 programming period highlights the need to focus on results. Mechanisms to ensure accountability and learning include the transferring of knowledge among parties and the improvement of performance by integrating feedback during and between investment cycles. Result and performance indicators shall help to provide a better understanding of the impact of Structural Funds interventions in the MS. “Because monitoring activities are not neutral and incentives effects are inevitable, the design of indicator systems should take potential gaming and strategic behaviour into considerations”<sup>145</sup>.

Monitoring of Cohesion Policy has to be understood as a comprehensive task going through all levels, i.e. from the programme level via progress reports at level of the PAs to bi-annual summary reports from the Commission to the Parliament and the Council. It is essential to see that the quality of information stemming from monitoring depends on the relevance and consistency of the indicator framework at programme level and across programmes and the quality management of data in the programme bodies. For obvious reasons the quality of monitoring information is decisive for the accuracy of evaluation on outcomes – in particular for large programmes involving numerous intermediate bodies.

The main partnership mechanism for the monitoring of programmes is the Monitoring Committee (MC). The composition of this Committee is decided by the MS and the MA while it is required to include the full list of partners specified in the partnership principle. The diverse involvement of different partners helps to support strategic dialogue among partners and to contribute to a shared ownership of the programme.

There is discretion in the type and number of actors involved in it and not all OPs include formal representation from all types of partners in all procedural steps. Especially non-state actors could be better involved which on the other hand creates longer debates and even more complex decision-making since decisions taken in the Committee are usually adopted consensually rather than through formal voting procedures<sup>146</sup>.

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<sup>145</sup> OECD 2009, Governing Regional Development Policy: The Use of Performance Indicators, OECD Publishing, doi: 10.1787/9789264056299-en.

<sup>146</sup> Metis, EPRC 2013.

The actual debate on progress in implementation within the MC is mostly driven by data from financial monitoring, i.e. the absorption of funds: this is understandable since automatic de-commitment is perceived as one of the most serious failures for programme management. The debate on programme outcomes is clearly ranked second in the perception of the MC (and quite often delegated to the evaluation).

One of the tasks of the MC is to examine the evaluations during the implementation of the programme. In addition, it is frequent practice to establish dedicated evaluation committees and networks where only government Ministries, departments and MAs rather than the broader partnership of OP stakeholder take part (*ibid.*).

### Evaluation

Evaluation requirements had been loosened in the period 2007-2013 and tightened again for the current period. The major novelty for the 2007-2013 period has been the introduction of evaluation plans in order to encourage programme management bodies to use the instrument of evaluation more strategically.

Evaluation or any kind of quality control requires an environment which respects its approach, values the outcome and is willing to get involved in a dialogue and a mutual learning process. Evaluation in Cohesion Policy often fails to follow this ideal path and gets stuck in the perception of a compliance exercise with limited added value for both sides, i.e. the programme management and the evaluator. Pre-conditions for any effect of evaluations are the back-up by the MA, the shared development of the key evaluation questions to be answered and the involvement of representatives from all stages of the programme cycle.

So far de facto hardly any examples have been made public where evaluation triggered internal learning processes among the actors in a programme management. Real changes in established (and encrusted) routines in most cases have rather been achieved by the independent audits (by the Audit Authority or the Commission) and its consequences.

### Role of the Certifying (CA) and Audit Authorities (AA)

The function of the AA is essential as an independent control body which is in charge of audit at three levels: the system, the system elements and the operations. In more detail the duties comprise:

- Providing an assessment on the general approach to the management and control system – in the period 2014+ this function is in hands of the so-called Designation Body but the task at hand is essentially the same.
- Elaborating an audit strategy (methodology, sampling techniques) which in the period 2007-13 had to be approved by the Commission and in the period 2014-20 has to be submitted only upon explicit request.
- Performing the system audit of the main elements of the system such as MA, CA and control bodies performing the verification of expenditure – this focuses on the one hand on the consistency and comprehensiveness of all templates, guidance and procedures and increasingly also on the qualification of the staff.
- Performing the regular sample audits at level of operations.
- Summarising the findings at system and operation levels in Annual Control Reports which are a pre-condition for payments of the Commission to programmes.

There have been many criticisms from programme management as regards the interpretation of the AA duties in the MS but it is evident that – given the volume of public funds in CP – an independent control body is essential in order to check the functioning of key elements in the system and to execute continuous control.

Despite the fact that general rules for the work of the AA are set-up and that international accounting standards should be applied in the end the role and approach of the AA has differed across MS. For instance the strengthened focus on policy outcomes means also a shift of attention for many AA which have previously focussed mainly on coherence and compliance of the system as well as the compliance of accounting at level of operations. Now, there is an increasing focus on aspects of cost-efficiency and relevance of the operations' outcomes. The strengthened focus of the AA on the outcomes has obvious consequences for the control bodies at programme level.

Major new challenges for the AA arise from two aspects:

- The increasing importance of anti-fraud and anti-corruption measures de-facto poses a new set of requirements, the need for new systemic approaches (e.g. work and cross-checking with data-bases etc.) and a comprehensive and coherent approach to risk assessment.

- The ‘electronification’ of accounting systems and invoicing poses new challenges since in principle it requires a thorough understanding of such system in order to assess whether systems are protected against manipulation.

In ideal terms the AA could strengthen its role as quality control for certain aspects of the policy delivery system. However, this would mean a certain shift of paradigm from the exclusive role of an independent authority to a body which also triggers learning cycles in order to improve the system.

## 3.2 Specific Governance Aspects related to LRAs

### The role of LRAs

The role and position of LRAs, their capacities and the actual policy impact at level of the LRAs have to be considered as a cross-cutting perspective.

*“The share of sub-national expenditure in total general government spending has increased in most EU countries over the past few decades as the role of regional and local authorities in delivering public policies has increased. Nevertheless, the share varies considerably between countries, largely reflecting differences in the institutional setting and the degree of decentralisation. Sub-national levels of government tend to be most important in Federal States, like Austria, Belgium and Germany or in countries like Spain and Sweden where there is high degree of decentralisation. It is important to note, however, that responsibility for undertaking expenditure is not necessarily synonymous with decision-making powers.”<sup>147</sup>*

However, the role of LRAs in Cohesion Policy is marked by huge gradients in the capacity to govern public investment policies of any kind across the EU:

- firstly in governance of ESIF and Cohesion Policy due to the differences in political-administrative systems across the EU;
- secondly in economic performance and development perspectives due to the increasing concentration of inhabitants – and thus economic capacities – in agglomeration or city areas on the one hand and declining rural economies on the other hand.

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<sup>147</sup> Sixth Cohesion Report, p. 142.



## Governance aspect

The sixth Cohesion Report sees the authority of EU regions growing:

*“There is a trend towards regionalisation in many parts of the EU. According to the regional self-rule index<sup>148</sup>, regions in many Member States have become more autonomous over the past 50 years, especially in Italy, Belgium and Spain as well as Scotland in the UK, in all of which there were high levels of self-rule at regional level.”<sup>149</sup>*

The aspect of governance essentially focuses on:

- the participation of LRAs in Cohesion Policy and
- the role of LRAs in an area or place-based policy approach since in this approach (or perception) the regional and local levels do represent the respective level of policy-making.

**Table 22. LRAs in Cohesion Policy – Aspects, roles and implications**

Aspect	Role and implications
Participation in Cohesion Policy	<p>Regions as Managing Authorities (MAs) or Intermediate Bodies (IBs):</p> <ul style="list-style-type: none"> <li>▪ MA: option to shape policy implementation but various degrees of actual self-government depending on the capacity to provide match-funding</li> <li>▪ IB: also large range of options to meet this function, i.e. from an intermediary which acts as neutral service provider to a decisive policy-making unit which tailors the Investment Priority to the actual regional/local needs</li> </ul> <p>LRAs as beneficiaries:</p> <ul style="list-style-type: none"> <li>▪ Local investment: either guided approach following priorities established at national/regional level or open competition among municipalities for funds (with policy outcomes depending mostly on the capacities in drafting and lobbying projects as well as providing or securing the required national match-funding)</li> </ul>
Territorial perspective of Cohesion Policy	<p>LRAs in the role of rather passive recipients or active policy makers:</p> <ul style="list-style-type: none"> <li>▪ Physical investment materialises at the local level; the decisive aspect of a genuine area- or place-based approach is the actual weight of the LRAs in the coordination of various policy approaches shaped by actors at national, regional and local level.</li> </ul>

Source: own considerations.

<sup>148</sup> The index captures the area over which a government exercises authority, the extent of this degree of independence and the spheres of action over which it is exercised (see sixth Cohesion Report, p. 172).

<sup>149</sup> Sixth Cohesion Report, p. 169.

## ESIF programmes managed by Regions

It is obvious that the role as an MA in an ESIF programme opens a comparatively broad room for manoeuvre in Cohesion Policy. When discussing ESIF Programmes managed by regions two distinct cases have to be taken into account:

- **Type 1:** countries with a long established tradition of federalism such as e.g. in DE, ES, FR or IT – in most cases these are programmes for more developed regions with a focus on support for competitiveness and RDTI – these regions benefit mostly from the longer-term budgetary commitment for specific development goals combining funds from the EU, the national and the regional level – the major added value is the stable longer-term financing framework.
- **Type 2:** countries which have seen a process of decentralisation in the past two decades such as in particular PL but also CZ and SK – for regions in these countries governing a Regional Operational Programme in terms of a stable longer-term funding instrument means a decisive shift in the capacity of self-government. These programmes are marked usually by a broad range of interventions<sup>150</sup> and in the period 2007-2013 have been marked by strong focus on basic local infrastructure which is now gradually replaced by more innovation-oriented types of interventions. Acting as MA for such broad programmes is quite challenging given the fact that the support structure in terms of intermediaries (agencies etc.) is less developed compared to regions in Type 1.

In EU 12/13 in terms of actual empowerment of the LRAs in programme implementation in the period 2014-2020 the most interesting example seems to be PL. In terms of safeguarding, funding for the least developed parts of Poland has taken an interesting approach with its overarching OP for the development of Eastern Poland: a major programme - under central management<sup>151</sup> - has been dedicated to the support of interventions for the most lagging parts of the country. Next to this programme in total 22 ROPs with the regions (voivodeships) acting as MA have been set up.

CZ has seen a process of re-centralisation in the implementation of programmes: in the period 2007-2013 so-called Regional Councils have acted as MA for eight ROPs established at NUTS-2 level<sup>152</sup>. In the period 2014-2020

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<sup>150</sup> E.g. the new set of ROPs in PL covers about 10 Thematic Objectives from RDTI to Social Inclusion.

<sup>151</sup> The Ministry of Infrastructure and Regional Development acting as MA.

<sup>152</sup> The decisive political-administrative unit being NUTS-3 – the so-called Kraj; this the Regional Councils combined in most cases representatives of two or more Kraj.

there is only one ROP which is governed by the Ministry of Regional Development.

In SK the general approach to the ROP has remained unchanged: the ROP is managed by the Ministry of Agriculture and Rural Development.

### **The economic capacity of the local level**

It is important to see that the capacity in project development and co-funding is also an essential aspect. In ROPs which run mainly on the basis of open calls for projects the capacity for project development and co-funding might become decisive for the success in the acquisition of projects regardless of the actual needs in the region. This tendency might be aggravated by lingering conflicts of interest with a growing role of political forces in crucial elements of the programme cycle such as selection.

Specific policy elements which require a stronger strategic element – such as the ITI – might help to counterbalance this tendency.

### **Key challenges of LRAs**

In general, the trend towards centralisation of EU economic and monetary policies brings about more challenges for LRAs. The tendency endangers the balance between national autonomy and the needs on the ground. This is probably most strongly felt by policy-makers at the local level in the least developed parts of a country where the lack of funds is often paired with the lack of effective policy levers thus fuelling a vicious circle and a quite passive role or non-participation in governance approaches.

Key challenges for LRAs in the programme cycle in Cohesion Policy relate to several aspects:

- The weak involvement in the programming process: In particular local authorities are not directly involved in the programming process – the role of associations representing the local level in the partnerships at national and programme level is usually quite weak.
- The lack of policy levers to actively coordinate development policies which are dominated by the national level resulting often in a lack of comprehensive and realistic development perspectives as basis for convincing project ideas.
- Low governance capacities mirrored in low capacities related to project development owing to a multitude of reasons be it their (small) size and

the resulting staff constraints, the competences and budgets available, the lack of support from the national level (which might lead to vicious circles in cases of countries which reveal persistent problems in the absorption of funds with adverse impact on LRAs).

- Low capacities in project implementation mirrored in problems to cope with the administrative workload, high risks related to procurement procedures, delayed implementation.

### *Procedural innovations implemented by the European Semester*

The six-month cycle in economic policy coordination brings two procedural innovations:

- A shift in the timing of the budgetary process – SGP and SCP must be submitted by MS before they are discussed by National Parliaments and translated into national legislation. Thus, specific ex-ante guidance (CSR) per MS can be provided by the Commission in order to strengthen economic policy coordination.
- Fiscal and structural reform plans are time-wise harmonised. SGP and SCP have to be submitted at the same time as NRP with the aim to ensure awareness on complementarities and spill-over effects across policy areas.

The decision to link the effectiveness of the ESIF expenditures to their respect of the annual CSR (the so-called macro-economic conditionality) was one of the most controversial aspects discussed during the adoption of the Common Provisions.

The CSR cover a wide range of policies. Beyond fiscal, budgetary, economic, and employment reforms, wage determination, education, pensions, health care, poverty and social inclusion are tackled. In this way, the scope of EU recommendations and surveillance was extended into policy areas which fall within the primary competence of MS (or often their social partners), where Union legislation is often prohibited under the Treaties<sup>153</sup>.

### *Considerations on centralisation of economic and monetary policies*

In general this aspect deserves particular attention in the discussion of future scenarios for CP as public investment policy.

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<sup>153</sup> Zeitlin et al. 2014, Socializing the European Semester? Economic Governance and Social Policy Coordination in Europe 2020.

Economic governance of respectively within the EU is currently rather reacting to phenomena of crisis and comprehensive responses to underlying major challenges have not been found yet. Major challenges in this regard are:

- Macro-economic imbalances between MS and the potentially adverse impact of economic policies between MS.
- The functioning of financial markets and their exacerbating role in macro-economic crisis.
- The consolidation of budgets of the MS.

Striking a balance between autonomously implemented and centrally coordinated policy is one of the main underlying questions in this debate.

With the obligations in the framework of the Stability and Growth Pact, i.e. the regular monitoring and reporting at level of MS in SGP/SCP first steps towards coordination of policies along a uniform set of indicators and an intensified debate on a country-specific pathways towards consolidation and stability have been taken. However, these developments are viewed upon critically in part due to methodological doubts<sup>154</sup> and in part due to its potentially adverse impact on the option for counter-cyclical public investment.

#### Financial markets and monetary policies

Related to financial markets an increasing role of EU's monetary policy as significant player in a global context is inevitable. Monetary policies targeting financial markets so far have been successful in limiting the impact of crisis and volatility of market developments but did have only limited success in re-establishing a more stabilising role of the financial market to the development of the real economy. Regulatory policies on financial markets so far have remained quite limited in scope and have opened intense debates in the dialogue between government, society and science.

From the perspective of LRAs financial markets might be perceived increasingly as a potential threat for their public investment policies; depending on the political-administrative system regions might be part-actors or just observers in this field, the local level cannot influence these policy developments.

Another important aspect is that the Euro is implicitly altering the governance architecture of the EU since the single currency has become an increasingly important policy rationale and might open new questions and divides within the EU. A stronger divide between the Eurogroup and the other MS might deepen the concerns of LRAs in non-members of the Eurogroup.

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<sup>154</sup> Cf. e.g. HM Treasury 2014, p. 2 – in particular in respect of ex-ante macroeconomic and fiscal projections and structural fiscal imbalances.

### Fiscal consolidation

The focus on fiscal consolidation in the recent past from the perspective of LRAs is also a potentially limiting factor for public investment policies since either LRAs are an active partner in the negotiations at level of MS in order to define the concrete pathway to consolidations or – in more centralised countries – LRAs will be confronted with the outcomes of such decisions. One has to see that the investments of LRAs focus on everyday life of citizens and basic amenities and thus such decisions do have immediate repercussions and in the end longer periods of austerity budgets will inevitably undermine local democracy and at the same time increase tendencies towards out-migration from challenged areas. Thus disparities between LRAs within the MS and thus also within the EU will increase.

### Economic policies

Major elements of economic policies such as tax and wage policies are in hands of MS. The debate on European economic governance in these terms is still at the inception stage and the principle of subsidiarity will prevail. As one report suggests: *The process of economic policy co-ordination blurs the boundaries between EU competences and domestic sovereignty, with the risk that policy co-ordination goes beyond clear EU competence*<sup>155</sup>.

At the current stage there is rather the risk that the focus on fiscal consolidation and monetary policies prevents any further debate on potential adverse impacts in one MS which arise from the economic policies of another MS. In CP one of the adverse consequences of such policies should now be avoided: CP investment should not contribute to the dislocation of major plants from one MS to the other.

Next to the strong role of MS in this field one has to see that the room for manoeuvre related to specific economic policies of LRAs becomes increasingly limited, be it regulatory or be it investment policies – in the latter case also due to the need for fiscal consolidation. As has been shown in many examples in the review of sectorial policies LRAs simply cannot influence major drivers such as pricing policies of production inputs (e.g. energy) and also costs for excellence in fields such as RDTI are rising; LRAs with diversified economies might be in a better position simply due to their more diversified assets (thus being in a better position to balance adverse developments in one sector).

In general one has to state an increasing complexity of economic governance in the EU and thus also an increasing risk of a tradeoff between policies debated

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<sup>155</sup> HM Treasury, 2014, p. 3.

and developed at EU level and the perception of LRAs. Here the EU institutions and representatives of MS do have to reinforce their capacities to make the overarching policy approaches more tangible for representatives of LRAs – in order to reduce the feeling of being a mere observer in an accelerating, complex policy vehicle.

## **The role of partnership-building and Multilevel Governance**

Despite the lack of a commonly agreed definition, MLG is generally understood as the participation of a range of different types of actors (public, private and societal) in policy-making and implementation through formal and informal means. The definition provided by the CoR<sup>156</sup> as a follow-up opinion to the White Paper ‘Building a European culture of MLG’ comes closest to the conceptualisation of MLG also in this study:

*“coordinated action by the EU, the Member States and regional and local authorities according to the principles of subsidiarity and proportionality and in partnership, taking the form of operational and institutionalised cooperation in the drawing-up and implementation of the European Union's policies”.*

Böhme et al.<sup>157</sup> identified five meta-dimensions of MLG, i.e. basic organisational principles, which need to be considered when analysing practices:

- Vertical coordination.
- Horizontal coordination.
- Functional, cross-territorial integration.
- Organisational capacity of territories.
- Mobilisation of stakeholder (i.e. non-governmental actors).

Vertical and horizontal coordination was tackled in chapter 2.1 (policy coordination at MS level). Likewise functional coordination, typically found in metropolitan areas or linking areas with territorial specificities, such as mountain or sparsely populated areas was described as being strongly dependent on the national institutional architecture.

Organisational capacity often relates to the adaptability of institutions and collective learning processes<sup>158</sup> and is still dependent on the institutional architecture at the national level<sup>159</sup>. A lack of organisational capacity has negative effects on the efficiency of policy implementation.

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<sup>156</sup> Committee of the Regions 2012, Building a European culture of Multilevel Governance: follow-up to the committee of the regions’ white paper, Opinion of the Committee of the Regions. Brussels.

<sup>157</sup> Böhme et al. 2013, study on promoting multi-level governance in support of Europe 2020, Inception Report, European Commission Regional and Urban Policy.

<sup>158</sup> Nordregio et al. 2013, ESPON TANGO. Territorial Approaches for New Governance, Draft Final Report, [www.espon.eu](http://www.espon.eu).

<sup>159</sup> OECD 2013, p. 51.

As a result of the emergence of the place-based approach to regional policymaking stakeholder mobilisation emerges. Through the mobilisation of stakeholders specific territorial knowledge can be accessed and the compatibility between pan-European overarching objectives and the territorial realities can be improved<sup>160</sup>. In particular the involvement of the private sector, e.g. through public private partnerships makes new funding sources accessible<sup>161</sup>.

## Peoples' perspective

The EU says on its transparency portal: *“The European Union's activities today affect millions of European citizens' lives. The decisions affecting them must be taken as openly as possible. As a European citizen, you have a right to know how the European institutions are preparing these decisions, who participates in preparing them, who receives funding from the EU budget, and what documents are held or produced to prepare and adopt the legal acts. You also have a right to access those documents, and make your views known, either directly, or indirectly, through intermediaries that represent you.”*<sup>162</sup>

Nevertheless in some fields and on some occasions European citizens do not fully trust in EU governance and institutions. In order to minimize this effect, European institutions have to react on the expectation of citizens and Cohesion Policy should be “used as a tool” for this. Linking the decisions of policymaking to citizens by increasing the link between effectiveness and democracy, transparency and bottom-up approaches might be an important action to take.

## 3.3 Financing Cohesion Policy

It is obvious that the question of financing needs to be seen in the context of the role of LRAs in Cohesion Policy as well as the different policy models in MS. However, it is the key question guiding all negotiations at all stages and it will be the more so in the coming years which will be marked by austerity budgets in many MS. Despite its comparatively small quantitative weight in economic aggregates such as the GDP or GNI the funds for CP are an essential element for public investment. One of the approaches to capture its actual weight – based on the concept of Expenditure for Development (EfD)<sup>163</sup> has estimated its average share in GDP with about 3% with a range between 1.5% (DK) up to 6.5% (CZ).

For many MS belonging to the group of EU12/13 in certain policy fields such as transport or environmental infrastructure the funding from CP has had a

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<sup>160</sup> Böhme et al. 2013.

<sup>161</sup> OECD 2013, p. 54f.

<sup>162</sup> [http://ec.europa.eu/transparency/index\\_en.htm](http://ec.europa.eu/transparency/index_en.htm).

<sup>163</sup> Cf. Metis 2011, p. 15.



dominant role and will continue to have so.<sup>164</sup> In the light of these general considerations on the weight of SF/ESIF as public investment source this chapter seeks to give an understanding of:

- The origin of CP funding.
- Main regulatory mechanisms determining the financing flows between EU and MS – in particular to those who benefit most from CP in financial terms, i.e. the Cohesion countries.
- Mechanisms fostering the financial discipline in CP.
- The perspective of LRAs.

European institutions. CP – which in the period 2014-20 has become the policy area with the highest funding appropriations among the EU policies - will be an implicit and explicit element in the debate about future funding mechanisms in the EU.

## Funding basis of EU Cohesion Policy

The budget of the EU is funded from the national contributions of MS. The revenues are coming mainly from the three sources as presented in the following table.

**Table 23. Revenues of the EU – funding basis of CP**

Source	Approximate share
GNI-based national contribution	75%
Traditional own resources of the EU <sup>165</sup>	15%
VAT-based own resources <sup>166</sup>	10%

Source: EC 2013a.

The Multiannual Financial Framework foresees a total budget of 1,082,555 MEUR<sup>167</sup> for the EU.<sup>168</sup> Thereof roughly 6.4% is spent for administration and about 94% for policies. The breakdown of the EU budget in major headings is as follows:

<sup>164</sup> Cf. Metis 2011, p. 16, shares ranging from 55% to even 90% (e.g. environmental infrastructure in HU) in the past period.

<sup>165</sup> Taxes raised on behalf of the EU, i.e. import duties.

<sup>166</sup> Taxes on EU citizens – proportion of the VAT; weighted average of VAT rates applied in the MS.

<sup>167</sup> Cf. EC 2013, p. 8; in current prices.

<sup>168</sup> Cf. EC 2013, pp. 8-9.

**Table 24. EU Budgets according to Budget Headings**

<b>Budget heading</b>	<b>Budget 2014-20 (in MEUR)<sup>169</sup></b>
<i>Cohesion Policy</i>	508,921
<i>Smart &amp; inclusive growth</i>	
Competitiveness for growth and jobs (COSME; SME programmes, H2020 etc.)	142,130
<b>Economic, social and territorial cohesion (ERDF, ESF, CF, CEF)</b>	<b>366,791</b>
<i>Agriculture</i>	420,034
<i>Sustainable growth</i>	
Natural resources – rural development (Pillar 2 – EAFRD, EMFF, LIFE+)	107,299
Market related expenditure and direct payments (Pillar 1 – EAGF)	312,735
<i>Other</i>	153,600
<i>(security and citizenship, global Europe, administration, compensation)</i>	
<b>Total</b>	<b>1,082,555</b>

Source: EC 2013a, p. 8.

Two major points stem from these considerations:

- The budget of the EU is tied to the economic capacity of the MS – the three main parameters, i.e. GNI, VAT and import duties levied by the EU, are directly linked to the economic performance of the MS – this is important to note since in the end the underlying rationale of CP is oriented on public investment as main policy lever to ensure economic, social and territorial cohesion in the EU but also as a policy means to be used countercyclical if needed (such as in the wake of the economic crisis); thus the long-term budgetary commitment and the concentration of funding should buffer phenomena of crisis in MS and ensure visible effects.
- In the period 2014-2020 Cohesion Policy (47%) has for the first time outweighed Agriculture (39%); this can be seen to some extent as a shift of paradigm in the major EU policies<sup>170</sup>.

<sup>169</sup> in current prices.

<sup>170</sup> When e.g. looking at the evolution of ERDF from a compensation fund for perceived disadvantages of the UK in the CAP to the key funds in the currently dominant policy area of CP (compared to CAP) – in the end this shift of paradigm documents the evolution over nearly four decades.

## Limits according to regulatory fiscal approaches

### Stability and Growth Pact

The Stability and Growth Pact is a regulatory policy approach of the EU which fosters the implementation of a fiscal policy posing limits on government deficit (3% of GDP) and debt (60% of GDP). All MS are obliged to submit a compliance report on an annual basis outlining the expected fiscal development for the n+3 years.<sup>171</sup> Since 2005 these programmes include also the Medium-Term budgetary Objectives (MTO) which are calculated for each MS and foresee the sustainable average limits for the structural deficit.

The Stability and Growth Pact and the fiscal path of the MS (laid down in SGP/SCP) is – in theory – one of the factors determining the room for manoeuvre in public investment thus having direct influence on public spending for CP. The past decade has shown that the Pact cannot be enforced against big countries and that so far also the initiated Excessive Debt Procedures did not lead to actual sanctions.

In the period 2014-2020 a link between the Pact and one of the core financial principles of CP, the additionality, has been established. The Gross Fixed Capital Formation (GFCF) is the unified public investment indicator<sup>172</sup> which is part of the SGP but also being used as benchmark in the verification of the compliance with the additionality principle. It refers to the net increase in physical assets.

### **Additionality**

The principle of additionality<sup>173</sup> means that EU Structural Funds may not replace the national or equivalent expenditure by a Member State. The Principle refers to those countries with significant shares of Convergence Regions thus being the MS which are most in need of support from CP. Compliance with the principle is verified at national level by the Commission, in cooperation with MS:

- in 2007-2013 for the regions covered by the Convergence objective,
- in 2014-2020 for those MS where less developed regions cover at least 15% of the population<sup>174</sup>; the verification is done at national level in case

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<sup>171</sup> Called Stability Growth Programmes (SGP) for MS in the Eurozone and Stability and Convergence Programmes (SCP) for the other MS.

<sup>172</sup> Defined by the European System of Accounts (ESA95).

<sup>173</sup> In the period 2014-2020 anchored in Article 95 of the CPR.

<sup>174</sup> 14 MS thereof verification at national level in BG, CZ, EE, LV, LT, HU, PL, PT, RO, SK, CR; at regional level in GR, IT and SI – cf. EC 2014a, p. 3.

such regions cover more than 65% of the population, at regional level in those MS where such regions cover more than 15% but less than 65%.

The additionality principle is subject to ex-ante, mid-term and ex-post verifications of the Commission.<sup>175</sup> The reference framework in 2007-13 have been the annual averages of structural expenditure<sup>176</sup> in real terms in convergence regions which had been compared to previous funding periods in convergence regions. These calculations took national specificities or exceptional levels of public spending<sup>177</sup> into account. The CF is not included in the calculations.

In practice the verification exercise for previous periods has encountered various difficulties<sup>178</sup> such as shortcomings in data comparability across MS, heterogeneity of the information provided, problems to capture all relevant expenditure and a significant work burden for both sides, i.e. EC and MS.

For the period 2014-2020 the GFCF is used as common indicator: it is understood that it is a proxy and represents a pragmatic compromise. But since it is being reported as part of the Stability and Convergence Programmes (SCP) on an annual basis the provision of data is secured. In those MS where the verification of the additionality principle is relevant, targets have been set in the Partnership Agreement (PA) outlining a long-term commitment until 2020, based on economic forecasts including the provision of annual spending profiles. The approach foresees financial corrections in case of differences of more than 3% compared to the target in PA. The target might be modified 2018 in the course of the mid-term review. The link between ESIF and sound economic governance has been put into focus and is now anchored in the CPR.<sup>179</sup>

So far in convergence regions the focus on investment has been on basic infrastructure – a fact which is important to note since this type of infrastructure reveals dominant shares of public investment. The broad brush picture of public spending in convergence regions in 2007-13 reveals a dominant share, i.e. almost 50% for basic infrastructure<sup>180</sup>, 30% for human resources and about 14% for productive environment. The results of the verifications document also the policy lever of SF/ESIF. E.g. according to the ex-ante verification of the Commission for the convergence regions in the period 2007-2013<sup>181</sup> it was

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<sup>175</sup> E.g. in the period 14-20 during negotiations for PA also setting the new baseline in GFCF (reference will be in most cases the annual average for 2007-2013), 2018 and 2023.

<sup>176</sup> Following the broad categories of basic infrastructure, human resources and productive environment

<sup>177</sup> E.g. German reunification or Olympics in GR etc., cf. EC 2009a, p. 5.

<sup>178</sup> EC 2009a, p. 11.

<sup>179</sup> CPR, Article 23 but also Annex III, determining the detailed scope and level of eventual payment suspensions

<sup>180</sup> Aggregate view for national funding and SF; the weight of SF in productive environment being more important than in basic infrastructure.

<sup>181</sup> EC 2009a, p. 3.

estimated that the 174 BEUR from SF will trigger 650 BEUR from domestic financial sources, i.e. a proportion of about 1 to 3.7 with significant differences between MS ranging from 1 to 1 in SK up to 1 to 17 in BE. The total amount was estimated to correspond to 5.6% of the projected GDP of the convergence regions. The final verification for the period 2007-13 will be done in 2016.

## Capping and Ceiling of ESIF support

In the past funding periods many MS have encountered difficulties in absorbing SF. One measure which has been introduced in the period 2007-2013 is a limit of the maximum support from SF/ESIF at level of the MS for the full funding period and a ceiling on an annual basis. For the period 2014-2020 it was initially intended to base it on a maximum share of a macroeconomic aggregate indicator, i.e. to cap it with 2.5% of GNI.<sup>182</sup>

- At level of the MS the final decision was to set the limit at allocations which are not higher than 110% of their level in real terms for the 2007-2013 period<sup>183</sup>.
- Annual appropriations are limited to a ceiling that would be fixed taking into account the GDP of *that particular MS*<sup>184</sup>.

## Capping of co-financing rates

The maximum co financing rate per Funds defines the major policy lever from a public national perspective since in the end it defines the minimum national match-funding needed for each programme and project. The maximum co-financing rates according to types of regions have been defined in the CPR<sup>185</sup>. The current approach is as follows:

*Table 25. Maximum co financing rates according to types of regions*

Fund / type of region	Specific Provisions	Maximum 2014-2020	Maximum 2007-2013
CF	---	85%	85%
Less developed regions	Average GDP per capita in 2001-2003 resp. 2007-2009 below 85% of EU-25 resp. EU-27 plus outermost regions	85%	EU 12/13: 85% Other MS: 75%
Transition regions acc. Art. 120, 3.b)	Average GDP per capita used as criterion 07-13 was below 75% of EU-25 but is above 75% of EU-27	80%	85% Spain conv.: 80%

<sup>182</sup> Cf. EC 2011.

<sup>183</sup> CPR, Preamble, Recital 85.

<sup>184</sup> CPR, Preamble, Recital 81.

<sup>185</sup> Cf. CPR, Article 120.

Transition regions, other	---	60%	75%
More developed regions	---	50%	50%
ETC (ERDF)		85%	85%

*Source: CPR, Article 120, Regulation (EU) 1083/2006, Article 52 and Annex III.*

The wording of the final provisions point clearly at the positions in negotiations and the compromises reached in the end.

However it is important to note that these maximum co financing rates refer mainly to projects which have the character of public infrastructure. In particular in the field of SME-support or RDTI maximum rates of state aid respectively public funding are defined according to provisions stemming from different considerations:

- E.g. in support to enterprises the Regional Aid Guidelines (RAG) but also sector-specific regimes which define ceilings according to regions, types of enterprises and in part also sectors – the criteria for as well as the designation of areas eligible for regional aid mark again the result of lengthy negotiations between MS and the Commission; important provisions e.g. on training for SME staff are also part of the General Block Exemption Rules (GBER).
- In support to RDTI the provisions as laid down in the GBER which define the maximum rates of support mostly according to types of RDTI with decreasing rates from fundamental over industrial research to prototyping.

### **Mechanisms aiming at financial discipline**

Improving discipline in the implementation of CP has become a key concern of the actors at European level. The measures fostering financial discipline rank among the most effective policy levers in order to avoid significant time lags in implementation. With the introduction of the so-called n+2/n+3 rule<sup>186</sup> in the period 2000-2006 a key element for increased discipline has been developed.<sup>187</sup> On the one hand the n+2/n+3 rule should be considered as pragmatic enforcement to a stable pace of programme implementation on the other hand it might support a tendency towards risk averse programme management, i.e. a focus on well-known project types which can be

<sup>186</sup> N+2-Rule: the annual tranche of a programme has to be spent at the latest two years after its allocation in the budget; e.g. the annual tranche in a programme for 2015 has to be spent until 2017 – if the payment target is not met, the corresponding budget share will be subject to automatic de-commitment.

<sup>187</sup> The complexity of ETC programmes has been taken into account in the period 2014-2020: now all ETC programmes are subject to the n+3 rule.

implemented in up to three years. Also financial instruments can be used to minimise the risk of automatic de-commitment at programme level.

In the period 2014-2020 three major new mechanisms have been introduced which should ensure a more transparent financial governance of ESIF programmes:

- The annual accounting, i.e. in particular the management declaration and annual summary issued by the MA; a measure meant to strengthen internal control of the MS and accountability in the shared financial management.
- The performance framework as part of each ESIF programme including financial indicators in order to foster commitment towards a stable programme performance but also to establish a clear basis for negotiations between EC and MS in case of lagging programme implementation; sanctions might range from payment suspension to financial corrections.
- The performance reserve<sup>188</sup>; set at 5 to 7% of the allocation per priority in a programme; the reserve shall be only allocated to programmes and priorities which have achieved the milestones in the performance framework.

### **Specific financing provisions as a reaction to the crisis**

It is important to note that to some extent European institutions allow for specific provisions in CP in order to react respectively counteract phenomena of crisis. E.g. in the period 2000-2006 some MS had been encouraged to use SF for mitigation actions after massive floods in several MS (AT, CZ, DE, SK, etc.).

In the period 2007-13 in the wake of the economic crisis the Commission approved reductions of national co financing for some MS (in particular ES, GR, IE, IT, LT) for the period 2011-12.<sup>189</sup> Additionally for the MS facing the greatest difficulties the co financing rates have been increased up to 95% depending on the type of intervention and the funds.<sup>190</sup> The Regulations governing the period 2014-2020 do also foresee limited options for specific provisions.<sup>191</sup>

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<sup>188</sup> Cf. CPR, Art. 22.

<sup>189</sup> Cf. EC 2013, p. 13; leading to a reduction of 19 BEUR or 3.7% of the planned investment.

<sup>190</sup> The so-called top-up facility has been initially intended to expire in 2013 but has been prolonged.

<sup>191</sup> Cf. CPR, Art. 24: option to increase interim payments to up to 100% of the co financing rate of the priority in the OP until end 2016 for MS in financial difficulties according to Regulations (EC) 407/2010 and 332/2002.

## **Trend towards greater flexibility and attractiveness of ESIF as financing instrument**

A notable trend in CP is the constant move towards more pragmatic but still safe handling of ESIF as financing instrument for a broader range of financing models. Often these measures seem small but still it underpins a trend away from ESIF as solely grant-based support which entails often a considerable administrative workload thus making it less attractive in comparison to other (national) forms of financing.

Examples which help to illustrate this tendency are:

- The introduction of financial instruments aiming at improved access to funding for various types of entrepreneurial activities at the same time offer the opportunity to generate sustainable instruments with an impact beyond the funding period; the intent is to offer – with the support of experienced actors such as banks and the EIB – competitive instruments to counteract the current challenges for young and small firms on the finance markets; it is also explicitly stated that audit work in such cases should focus on the programme management bodies in charge of the intervention in order to avoid disproportionate administrative burden for beneficiaries.
- The flat-rate approach for operations generating net revenues in order to have an alternative to the rather sophisticated calculation methods<sup>192</sup> applied in previous periods as well as to relief the burden related to the monitoring of revenues.
- Shortened periods related to the sustainability of SME investment (from 5 to 3 years) in order to adjust to the current reality of a comparatively quick succession of economic up- and downturns and the repercussions on investment cycles.

## **The perspective of LRAs**

### Role of LRAs as investors

The investment and funding capacity of LRAs depends largely on the political-administrative system of the MS. The distribution of competencies and the tax system governing the distribution of taxes, the existence of mechanisms for tax equalisation between different tiers of government – all these are the factors

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<sup>192</sup> The so-called funding gap method and calculation of discounted revenues.



determining the actual weight of the LRAs in policy-making and thus also in CP as public investment policy.

In general investment by LRAs is characterised by a significant share of amenities which are close to the every-day needs of citizens. Investment by sub-national governments in the OECD shows the following rough breakdown:<sup>193</sup>

- 37% for economic affairs and infrastructure (transport, communications, energy, construction).
- 23% for education.
- 12% for housing and community amenities.
- 9% for general public services.
- 6% for social protection and health.
- 6% for religion and culture.
- 4% for environment protection.
- 3% for others

Investment in infrastructure is one aspect; the second key aspect is the long-term financing of maintenance and operation of the infrastructure. The latter is also growing burden and might become critical in case of municipalities facing the adverse consequences of demographic change: e.g. public transport infrastructure in a mountainous region confronted with out-migration costs more and brings less compared to the same facility in a dense urban region or the decline might even require the costly down-sizing of infrastructure.

It is important to note that regarding the financing capacities of LRAs one has to differ between the local and the regional level. In a study on the complementarity of national and community interventions related to CP the situation has been summarised as follows:<sup>194</sup> *“High and visible spending levels at regional level are a characteristic feature of a small group of MS. According to the EC’s 5th Report on Cohesion on EU average the subnational level accounts for 28% of public expenditures. Countries with highest shares are those where local and regional levels play a crucial role in the provision of public services and goods: Leading countries in the EU are DK (45%), ES and SE (about 40%) and DE (35%). AT, BE and FI also reveal shares above 30%.*

*The number of countries with significant spending levels of a regional level (i.e. between local and national level) is even smaller: BE (regions), ES (comunidades autónomas), DE and AT (both Länder). Among the new Member States CZ, PL and LV show shares close to 25%.”*

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<sup>193</sup> OECD, 2014, p. 5.

<sup>194</sup> Metis 2011, p. 17.

### The influence of economic development

The financing capacity of LRAs is closely linked to economic performance and development perspectives which in the end determine the capacity of LRAs in the provision of utilities and services. Maintaining and expanding infrastructure in periods of budgetary constraints will become increasingly difficult even for LRAs with a comparatively sound economic standing and for LRAs in challenged regions it will mean complete dependence on transfers from the national level.

One can assume that the persistent crisis will tend to increase and sharpen these gradients between LRAs as well as to narrow the room for manoeuvre in policy-making in particular for the most challenged regions.<sup>195</sup> Public investment has dropped on average by 20% in the period 2008 to 2013, with a particularly marked drop in Greece, Spain and Ireland (by 60%).<sup>196</sup> LRAs are responsible for almost two thirds of all public investment in the EU and thus one can guess the impact at local and regional level which these cutbacks in public investment have had across the EU.

### LRAs and match-funding for CP

When looking in more detail into the need for match-funding for CP at level of LRAs one has to be aware of the fact that the major part of funding goes to less developed regions. The following table outlines the breakdown according to the objectives of CP and thus also according to the types of regions.<sup>197</sup>

**Table 26. Community Funding according to CP Objectives**

<b>Fund / type of regions</b>	<b>Funding 2007-2013</b>	<b>2014-2020</b>
Cohesion Fund	58.3 (23.2%)	66.3 (20.6%)
Convergence – less developed regions (below 75% of GDP/capita)	177.1 (55.6%)	164.3 (51.0%)
Phasing-in; phasing out - transition regions (75% to 90%) In 2007-2013 part of RCE	<i>Convergence: 12.5</i> <i>RCE: 10.3</i> Total: 22.8 (7.2%)	32.1 (10.0%)
Regional Competitiveness and Employment (RCE) – more developed regions (more than 90%)	49.1 (15.2%)	49.1 (15.2%)

<sup>195</sup> I.e. those regions challenged by economic and demographic decline which tend to be trapped in a vicious cycle.

<sup>196</sup> Sixth Cohesion Report.

<sup>197</sup> A new element in CP 2014-2020 are also the minimum target shares of ESF spending according to types of regions as stipulated in the CPR ranging from 25% in less developed regions to 52% in more developed regions.

Outermost and sparsely populated areas (SE, FI)	3.3 (1.0%)	1.3 (0.4%)
ETC	7.7 (2.4%)	8.9 (2.8%)
<b>Total</b>	<b>318.3 (100.0%)</b>	<b>322.0 (100.0%)</b>

*Source: Regulation (EU) 1083/2006, Articles 18 to 20, CPR, Art. 92, own calculations.*

Behind this breakdown a variety of challenges related to the provision of match-funding exists. Examining the situation in all MS would exceed the scope of this study but a couple of examples should help to understand that CP – in particular from the regional perspective – is based on fundamentally different funding mechanisms and thus also approaches to governance.

The least challenge from the perspective of LRAs in providing match-funding for CP is most probably given in **federal systems** such as in DE which has a substantial share of funding in transition regions and more developed regions. DE uses the ESIF as part of a subsumed system, i.e. ESIF become part of an established funding system with clear-cut roles of all tiers of the government. The major asset of CP in such a system is the shared long-term funding commitment which usually exceeds other periodicities such as e.g. the negotiations in tax equalisation systems.

None of the large net-recipients of CP-funding as well as none of the Cohesion Countries<sup>198</sup> can be ranked among the federal systems which are marked by comparatively strong LRAs.

A further group of MS – receiving substantial funding from CP – includes countries with a long tradition in CP: these are ES, IT and PT. In those countries exists a large number of ROPs (for ERDF and EAFRD) next to a limited number of OPs at national level. In particular Spain and Italy represent regionalised or highly devolved systems where LRAs have significant responsibilities in decision-making and implementation. E.g. in Spain the regions (autonomous communities) have differing status of independence and next to Community funding a national equalisation fund for support of the less developed regions has been established.<sup>199</sup> The resulting funding arrangements between national and regional levels are marked by a great variety.<sup>200</sup> Also in Italy a national funding instrument has been established in order to strengthen the funding capacity of the less developed regions.<sup>201</sup>

<sup>198</sup> 2014-2020: BG, CR, CY, CZ, EE, GR, HU, LV, LT, MT, PL, PT, RO, SK, SI.

<sup>199</sup> So-called Inter-Territorial Compensation Fund.

<sup>200</sup> EPRC 2006, pp. 70-74.

<sup>201</sup> Fund for Underutilised Areas (Fondo per le Aree Sottoutilizzate – FAS; established in 2003).

Finally the situation of those MS of among the group of EU12/13 with large population shares in less developed regions should be highlighted: these are CZ, HU, PL, RO and SK. Most of these countries can be described as unitary states albeit with quite heterogeneous features when it comes to the governance of LRAs. Two broad categories in the group of EU12/13 can be distinguished:

- Some countries (CZ, PL, SK) have established **decentralised systems**, where regions may have elected parliaments but quite limited budgetary powers.
- Countries with a **strongly centralised system** such as BG (statistical regions), HU, RO or CY, EE, LV, LT, SI, MT as very small countries without regional authorities.

These differences are also reflected in the programme architecture (e.g. PL has 16 ROPs whereas CZ<sup>202</sup>, RO and SK have established one ROP as large ERDF-programme. Basically the fact that one large ROP exists means that there might be underlying funding targets according to regions and regions have a role in decision-making but it is not the type of long-term contract between national and regional government as e.g. in federal systems.

The funding system in countries such as CZ, HU and SK usually foresees that a fixed percentage of the national public match-funding is provided by the national level and another (usually smaller) percentage has to be provided by the beneficiary such as a LRA. Several aspects deserve particular attention:

- In many policy fields the approach to ROPs does not foresee a clear element of a ranking according to needs but rather opens a market for beneficiaries where the performance is linked to the capacity in project development (which might in turn require also funding).
- The provision of own resources is usually a small but might be in case of challenged regions a visible problem.
- The key challenge stems from long periods of pre-financing which might pose serious challenges in case of numerous ongoing projects.
- An obvious further challenge in systems with low own capacity of LRAs to generate funding capacities through tax revenues or transfer is the long-term maintenance of infrastructure upon investment.

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<sup>202</sup> It is interesting to note that in CZ the approach to ROPs has undergone a re-centralisation compared to the period 2007-2013.

PL has developed a model: a specific feature of the implementation of CP in PL are the framework agreements between the central state and the voivodeships; these *regional contracts have served as an instrument to facilitate central spending on regional projects or to co finance Cohesion Policy projects.*<sup>203</sup> PL has to some extent adjusted the approach developed in FR and thus seeks to strengthen the commitment across tiers of the government.

### *Increased participation of the private sector as alternative*

Given the budgetary situation in many MS an increased mobilisation of private funding might be an interesting option: *Involving private actors and financing institutions in the investment should be a way to strengthen the capacity of government at different levels and bring expertise to projects through better ex-ante assessment, improved analysis of the market and credit risks, and achieving economies of scale and cost-effectiveness (OECD, 2014, p.10).*

However, at first hand the options linked to this approach appear to be quite limited for those regions which face probably the most pressing need for new funding sources. This goes back to a number of reasons:

- Less developed regions are marked by the need to catch-up in basic infrastructure which are mostly considered as public amenities; infrastructure or approaches which are of interest for private funding such as ports, airports, RDTI infrastructure or energy contracting are characteristics of more developed regions and thus implicitly having a better economic footing.
- Attracting private funds and governing the resulting approaches such as PPPs requires experience and capacities in LRAs – a capacity which is usually not available in the administrative structures in the most challenged areas.

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<sup>203</sup> Cf. EPRC, 2011.



## **4 Synthesis and Conclusions**

### **4.1 Gaps, Trends and challenges with impact at regional and local level**

This chapter will summarise on the major trends in the three traditional sectors and outline the challenges and needs for Cohesion and Cohesion Policy.

**Table 27. Major trends in social, economic and territorial cohesion per sector**

Sector	Major trends	Social Cohesion	Economic Cohesion	Territorial Cohesion
Agriculture	Intensification and polarisation, Liberalisation and global competition Cost pressure, Environmental externalities, Emergence of agro-environmental and ecosystem services approaches Depopulation and marginalisation, Changes of land uses (abandonment, use for leisure)	Need for diversification and supply of employment and production processes, Need for safeguarding education and training opportunities, Preservation of a just taxation base,	Need to adapt to the global competition, Need to ensure sources for capital investments, Need to enable integration and exploitation of technological advances, Need to decouple growth from (imported) resources,	Need to introduce area based policy approach (instead of sectoral), Need to enhance centre-periphery cooperation, Need to overcome locational disadvantages and/or valorise local advantages, Need to adapt infrastructure to the trends and ensure cost-efficient connectivity and services, Need to stop marginalisation and out-migration, Need to integrate migrants
Industry	Integration in global value chains, Standardisation, Global competition, Interweavement with services, Division of labour and regional demand for specific skills, Increasing disparities for peripheral areas, Polarisation effects and vicious circles, Staggering resource consumption, Rehabilitation costs	Respect of minimum social standards, Need to enable local livelihoods, Need to address increasing social segregation and spatial polarisation, Need to accommodate the “globalisation losers” and the marginalised groups,	Need to provide or attract highly skilled/diversified personnel, Need to provide cost-efficient services of general interest and infrastructures and ICT, Need to provide for a framework that favours innovation (standardisation, IPR protection, financing, support etc.) Need to provide for compensation schemes for the provision of public goods and safeguarding of common-pool resources	
Services	Tertiarisation, Increased demand due to increased living standards and production processes, Innovation drive creating new services, Delocalisation of industries, Increase of precarious jobs, Growing demand for social services, Growing demand for labour market interventions	Importance of social innovation and effective governance modi,	Need for Innovation Need for Standardisation	



Perspectives for LRA Action			
Regulatory acts	Definition of required minimal skills	Definition of operating conditions (e.g. permits) Obligation for minimal standards and CSR provisions Protection of employee rights	Definition of spatial opportunities and restrictions, Definition of minimum standards for each territory
Incentives	Provision of infrastructures Fostering of Social Innovation and governance Incentives to invest in skills Incentives for the development of services,	Provision of fiscal incentives, Provision of infrastructures	Provision of fiscal incentives, Provision of infrastructures, Provision of flexible infrastructure to respond to local needs,
Information and Motivation	Fostering of Social Innovation and governance Foster CSR,  Strategies to attract stakeholders in becoming active	Marketing/Branding	Marketing/Branding

*Source: own considerations.*

As it becomes evident in the table above the scope of LRA action is broad. Classical approaches like regulatory provisions are still wide-spread; however they are becoming less effective in the globalised world or tend to focus on minimal requirements, hence lacking the potential of actively influencing a development and growth strategy. In the field of “incentives” LRA can become more active, however guarding on the long term sustainability of their regions and the avoidance of social and economical erosion.

In the table below the role of the EU sectorial policies is summarised and the opportunities and implications for the tasks for LRA are highlighted.

**Table 28. The role of EU sectorial policies and opportunities and implications for the tasks for LRAs**

<b>Sectorial Policy</b>	<b>Major Trends</b>	<b>Social Cohesion</b>	<b>Economic Cohesion</b>	<b>Territorial Cohesion</b>
Environment, climate change adaptation, low-carbon economy and resource efficiency	The Water Framework Directive is the cornerstone of water resources protection demanding an integrated long term ecosystem approach; Waste is turned into a resource; Waste minimisation is preferred over waste management and disposal; Climate change affects the availability of water resources ; Biodiversity as a guarantee for the sustaining of ecosystem services and human welfare; Resource efficiency is a global competition factor affecting all aspects of production and consumption	Restrictions/pricing on resources use and disposal Alternative job opportunities, Spatial planning and zoning, Risk management and voluntary organisations, Creating local green markets	Restrictions/pricing on resources use and disposal Demand for Eco-innovation, technological solutions, monitoring etc. Demand for innovative and efficient management practices Investments for climate change mitigation and adaptation Spatial planning and zoning, risk management and location selection, Response to degradation of ecosystems and the need to adapt to the loss of environmental public goods Promotion of partnerships for resource efficiency and definition of standards	Integrated management approaches beyond administrative borders Construction and operation of public utilities networks, physical infrastructure and other related works Spatial planning and zoning, Risk management, Valorisation of biodiversity and natural heritage
Labour market and social policies, health care	Increasing unemployment; Increasing atypical forms of employments; Polarisation and accentuation of poverty risks; Demographic transition and ageing society; Need for flexible social services, e.g. childcare; Migration.	Provision of locally adapted social services Provision of support services for escaping poverty traps	Enabling work life balance Enabling economic activity and employment of disadvantaged groups Creation of incentives for entrepreneurship, employment etc.	Mobilisation of area based tools such as CLLD, IT etc.

Education and qualification	Young unemployment as a result of poor skills; Mismatch of labour market needs and education/training offerings; Education and training as prerequisites for social integration; Poor qualifications recognition of migrants.	Local adaptation of offerings	Local employment agreements (e.g. TEP)	Mobilisation of area based tools such as CLLD, IT etc.
Research and Innovation	Increasing dispersion of business activities; Competition for high value activities in Global Value Chains; Accelerated knowledge flows between interconnected knowledge hubs and polarisation; lagging behind regions cannot catch-up;	Provision of skilled labour forces Attractiveness as residence choice for highly skilled R&D personnel	Provision of locations, Spatial planning and zoning, location selection support, Development of auxiliary services (e.g. non basic sector)	Management and implementation of tools like the RIS3 Creation of “innovative” regions in the context of the JRC key elements (niche products, securing of resources and conditions, overcoming path-dependency)
Network development and infrastructure	Investments in the TEN (differentiation among core and comprehensive network) Mobilisation and coordination of investment sources, Increase in traffic flows, “containerisation” and multimodal hubs, New logistic concepts and need to keep pace with capacities Increasing environmental considerations	Provision of “accessibility justice”	Provision of infrastructure as a location selection factor Integrated management “real time” approaches Integration of energy supply and demand in the infrastructure provision and location endowment	Integrated management approaches Construction and operation of public utilities networks, physical infrastructure and other related works Spatial planning and zoning, Risk management,

SME policy	<p>Recognition of the role of SMEs</p> <p>Extensive specific administrative burden for SMEs.</p> <p>Difficulties in access to finance</p> <p>Limited access to public procurement</p> <p>Modernisation of bankruptcy procedures and abolition of social and administrative stigmata</p> <p>Entrepreneurial education</p> <p>Integration of SMEs in Global Value Chains</p>	Facilitation of entrepreneurship	<p>Provision of locations,</p> <p>Spatial planning and zoning,</p> <p>location selection support,</p> <p>Development of auxiliary services (e.g. non basic sector) and intermediaries</p> <p>Provision of loan facilities</p>	<p>Territorial partnerships</p> <p>Provision of attractive environments</p>
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*Source: own considerations.*

## **4.2 Effectiveness, Efficiency and Governance of Cohesion Policy at regional and local level.**

Considering the whole programme implementation of common provisions and the common strategic framework in the 2014-2020, the MS had the general attitude not to change very much from the 2007-2013 period. The new requirements were reluctantly implemented and especially the integration of EAFRD and EMFF with ERDF, ESF and CF induced different reactions. MS with a comparably large budget for Cohesion Policy instruments generally welcomed the integration of funds. On the other hand, in other MS the integration “was more of an exercise on paper, and it is doubtful whether there will be any coordination at the level of implementation of OPs<sup>204</sup>”.

### **4.2.1 Mechanism to ensure respectively improve policy delivery**

The translation of strategic papers such as the Europe 2020 strategies and comprehensive guidelines into national strategies shaped by domestic policy bears the trade off between strategic guidelines at EU level and the reality of Cohesion Policy as well as the actual use of Structural Funds at local level.

Firstly, challenges are obvious during policy coordination: The gap between the Country Specific Recommendation and national strategic and programme documents as well as the EU legislative package comprised different interpretations at national level. The regular verbal communication between MAs, desk officers and different stakeholder on the one hand may create misunderstandings compared to written comments. On the other hand, it is a necessary part of policy coordination in order to improve results and ensure accountability on all sides.

In centralised MS vertical policy coordination from central level to LRAs implies difficulties as a result of information gaps and awareness with regards to each government priorities. Mechanism to strengthen vertical coordination across levels of government such as national investment strategies, territorial representatives, regional development agencies and formal agreements should be considered in order to strengthen the role of LRAs. In particular the principle of co-financing, formalised consultation processes, dialogue platforms and informal coordination arrangements help to improve the involvement of LRAs in Cohesion Policy.<sup>205</sup>

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<sup>204</sup> Metis, 2014, Implementation of Cohesion Policy 2014-2020: Preparation and administrative capacity of Member States, European Parliament Policy Department B: structural and cohesion policies. (p. 54).

<sup>205</sup> OECD 2007.

Administrative and regulatory obstacles hinder efficient coordination not only vertical but also horizontal – cross boundaries between established players in their political-administrative systems. Legal and administrative obstacles are rooted in the politically defined land borders of Europe: Different individual governance and legal systems directly meet at the political borders which can produce “closure effects” for all sorts of economic, social, inter-cultural or inter-personal exchange relations across EU borders<sup>206</sup>.

The common provisions implemented in the 2014-2020 period may increase cross-fund investments that have remained an exception in the preceding period. Moreover, the European Code of Conduct on Partnership (Art. 5 CPR) shall help MS organizing a meaningful partnership with relevant stakeholders. Already established steps are the ex-ante evaluation as well as interservice consultation.

In the current period, multi-fund programming enhanced general policy coordination and reduced the number of OPs and therefore the administrative workload.

Fund-specific regulations provide for the translation of thematic objectives into investment priorities which can be seen as objectives leaving flexibility to design the optimal mix of actions.

The introduction of ex ante conditionalities supports the development of strategic guidance in key sectors as a pre-condition for Union support.

In order to increase the thematic focus and bring ESIF in line with Europe 2020 rules on thematic concentration, i.e. obligatory financial allocation which gives the thematic concentration a much higher enforcement were introduced.

EU policy implementation is mostly considered as national agenda in line with the subsidiarity principle. Therefore, this stage allows the highest flexibility in adapting to political administrative systems of the MS. The management structures as well as the scale and thematic content of the programme influence the number and types of actors involved.

With regards to project assessment experience shows different assessment procedures in dependence on the broadness and scope of the OP as well as on the type of MS. Different types of risks and uncertainty associated with public investment exist at the early stage of the investment cycle as part of the appraisal. Such fiscal, political, social and environmental risks should be re-evaluated as new information becomes available<sup>207</sup>.

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<sup>206</sup> ESPON 2013 project „GEOSPECS“.

<sup>207</sup> OECD 2014, p. 10.

MLG that can contribute to greater policy effectiveness, commitment and ownership in decision making and of policy outputs can be facilitated by regular information exchange and targeted training measures.

The moral hazard problem refers to the risk that projects with low or no added value are being implemented through ESIF programmes. Containment can be ensured through mechanism such as the building up of capacities and expertise in management, transparency and tangible selection criteria, analysis and guidance, MA's responsibility and quality control.

One of the most demanding tasks for most MS is the setting-up of effective and efficient control bodies which are in charge of the financial control task. The time spans from submission of payment requests to closure of control routines are often much longer than expected and prescribed<sup>208</sup>. A set of regulations for the 2014-2020 period has introduced new approaches to simplify the verification process such as standard unit costs, lump sums and flat rates. Now, MS have to take up these options and integrate it to the national eligibility rules.

Debates in policy delivery tend to focus on the absorption of funds: automatic de-commitment is perceived as one of the most significant failures for programme management. In the main partnership mechanism, the Monitoring Committee, thus the discussion of programme outcomes is clearly ranked second and often delegated to the evaluation.

Evaluation in Cohesion Policy often fails to facilitate a dialogue and mutual learning between the evaluator and the authority, project or institution to be evaluated. Pre-conditions for effective evaluations are therefore the back-up by the MA, the shared development of the key evaluation questions to be answered and the involvement of representatives from all stages of the programme cycle.

#### **4.2.2 The role of financing and funding mechanism**

The period 2014-2020 is marked by the fact that for the first time CP has received a higher allocation than CAP. The funds for CP (as well as those for the CAP) are tied to the economic performance of the MS. Thus a long-term crisis in the EU will have inevitable consequences for the funding of CP – and thus the underlying options to use it as a countercyclical investment instrument. In this period the MS with substantial share of less developed regions will come under a closer scrutiny from the EU: in particular the monitoring of the implementation of CP and the monitoring of the MS's economic performance in terms of the Stability and Growth Pact have been tied together. As a reaction to

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<sup>208</sup> In the period 2007-2013 a limit of three month has been introduced.

the economic and financial crisis in the period 2007-13 a set of specific measures for MS in economic difficulties has been introduced.

The bulk of funding within CP goes to the less developed regions (about 50% to the regions, 20% via the CF). Under the assumption that the current mechanisms are being continued large-scale changes after 2020 might stem from the re-classification of the (substantial) transition regions in ES and DE and the economic developments in PL.

Lagging disbursement of funds has led to the introduction of mechanisms to ensure financial discipline. The rule on automatic de-commitment ranks among the most visible policy levers of the EU within CP – it has immediate and substantial impact on programme management. One has to see that in the period 2007-13 some Cohesion Countries have been de-facto net-contributors for limited periods due to the extremely slow up-take of programs in CP. A potentially adverse systemic impact of the de-commitment rule is that it might support a tendency towards standard types of projects with low degrees of implementation risks but also low potentialities to trigger off new developments.

With a view to the role and perspective of LRAs the economic capacity i.e. the provision of match-funding and the capacity to pre-finance long periods until reimbursement for operations might become even more decisive in the period 2014-2020: thus in particular small LRAs in less developed regions might encounter additional disadvantages in case of programmes which do not foresee a clear ranking of projects according to needs.

Any debate about the future of CP will start at the funding. The underlying mechanisms are quite complex and represent compromises after long negotiations. The funding mechanisms can be understood as control levers of a quite sophisticated system and changes in one position will have repercussions on other system elements. In principle one could imagine two scenarios:

- Either the whole system of CP undergoes a complete change after 2020, i.e. with a substantial re-definition of all mechanism – which is most probable in a scenario where funding is drastically reduced or
- The current system is more or less maintained and adjusted – in this case there are numerous policy levers which could be re-positioned such as in particular the allocation to the Funds, the distribution between types of regions (more/less developed), the co-financing rates, the advance and interim payments of the EU to MS, etc.



### 4.2.3 Strengthening the role of LRAs

Regions and places are increasingly considered as the key level for establishing more efficient policy coordination. Their capacities to govern EU public investment policy are strongly influenced by the differences in political-administrative systems across the EU. Moreover, they are affected by external economic and social pre-conditions such as demographic challenges and economic decline in rural areas and population growth and financial accumulation in growing urban areas.

The role of PAs and OPs in strengthening the consistency and integrity between the funds as well as EU and national strategies and policies must be considered when improving the participation of LRAs in Cohesion Policy. Closer cooperation between different regional and local partners in MS as well as the involvement in PA and OP development is crucial not only for policy coordination but also for Structural Funds implementation during the other policy stages.

The participation of LRAs in Cohesion Policy by representing the MA or Intermediate Bodies offers the possibility to shape policy implementation or to tailor the Investment Priority to the actual regional/local needs. In addition LRAs can take the role of passive recipients or active policy makers. The decisive aspect of a genuine area- or place-based approach is the actual weight of the LRSs in the coordination of various policy approaches shaped by actors at national and local level.

Regions governing Regional OPs in countries with a long tradition of regional ESIF Programmes (DE, ES, FR, IT) benefit from the longer-term budgetary commitment for specific development goals combining funds from the EU, the national and the regional level.

On the other hand, regions governing a Regional OP in countries that experienced a decentralisation process (CZ, PL, SK), the stable longer-term funding instruments lead to a decisive shift on the capacity of self-government. In those regions, frequently financed local infrastructure is now gradually replaced by more innovation-oriented and broad types of intervention. This entails all challenges as a result of less developed intermediaries whose support of implementation in experienced regions is an important success factor.

Structural Funds policy coordination anchored at MS level implies (a) the focus on strategic issues and guidelines to support the pace of implementation and (b) the lack of options and communication routines for a regular exchange between the operative units. Here, it might be wise to involve LRAs in inter-ministerial committees linking sectoral ministries that coordinate ESIF at national level in

order to improve operative management of the programmes. In countries where no such committees exist a strong involvement in the Monitoring Committees as coordination mechanism of ESIF is recommended.

Another very important aspect is the governance capacity of the local level. The capacity for project development and co-funding might be decisive for the success in the acquisition of projects often regardless of the actual needs or nay prioritisation. It remains to be seen whether the introduction and implementation of the very strategic CLLD and ITIs meets coordination and territorial challenges more sufficiently.

Moreover, the weak involvement of local authorities in the programming process as well as their weak representation in the partnerships reinforce their low governance capacities and capacities in project implementation. The adaptability of institutions and collective learning (organisational capacity, cf. Böhme et al. 2013) processes is still dependent on the institutional architecture at national level.

The OECD describes the term capacity referring to the “ability to adhere to good practices in the design and implementation of public investment“. Moreover, it points out that “regional or local governments may lack the capacity to implement the policies needed to foster regional growth, though their knowledge and preferences remain essential to informing place-based policies”<sup>209</sup>.

The lack of institutional capacity should be tackled by helping the MS and various partners to build their own strategy.

The investment in capacity building should be increased in qualitative terms. Therefore, the focus can be on public innovation policies as trainings on “assessment risks”.

From the structural perspective, implementation rules should be simplified and the current bureaucracy must be reduced through innovative approaches and improvement of internal and external communication channels.

The place-based approach facilitates the mobilisation of stakeholders (including private sector) and their specific territorial knowledge. Thus, the compatibility between pan-European overarching objectives and the territorial realities can be improved<sup>210</sup>. In addition, the linkage of policy decisions and the peoples’ perspective must be increased by linking effectiveness and democracy, transparency and bottom-up approaches.

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<sup>209</sup> OECD 2013, p. 25.

<sup>210</sup> Böhme et al. 2013.

A territorial approach of foresight could be followed in order to identify the challenges of each territory and help defining strategic goals of a specific region in relation to EU policy. The relationship between the finances of the Cohesion Policy and the sub-national budgets, including the Stability Pact provision has to be tackled.

In relation to EU funding eligibility, conditionalities that increase the regional policy in the MS could be an instrument to meet regional needs. Moreover, it might be worth considering the creation of a single EU mono-Fund that supports regions according to its specific needs and challenges.

Also the advantages and disadvantages of central vs. decentralised implementation of sectoral vs. integrated programmes are of high importance when arguing for more sub-national support.

In terms of the quality of investments and projects' results the impact in the real economy are still difficult to measure. The role of different actors in delivering Cohesion policy objectives as well as the modes of decision-making and public participation has to be tackled.

Models of partnership and MLG decision-making have to be considered asking for the different results, the level and leverage of co-financing as well as its providing authority or institution and amount.

The implementation of a proportional audit system based on a new partnership approach and on the MLG principle is something to be elaborated. A future evaluation system should be based on more suitable indicators and the effectiveness has to be linked to a result-oriented approach.

With regards to accountability, transparency and result-orientation, the promotion of further exchange of best practice and concrete cases among regions is of great importance.

There is still a sharp economic divide between regions across Europe. EU Cohesion Policy in many cases is dedicated to work on pre-conditions – such as upgrading basic infrastructure – in order to enable access to or to allow for a certain geographical spread of growth next to capital or other economically successful areas.

It is important to ensure that LRAs are adequately involved in the design and the delivery of the national responses to the strategic framework of the EU for the forthcoming period. This will follow established routines in countries with long-standing tradition of regional self-governance but it constitutes a significant challenge for some of the new MS, where the involvement of regional bodies

still is in a fairly early stadium or no self-governing regions exist. In the latter case the strategic gap between national policy objectives and local interventions might be even wider. These points at the need that the national level and the EU - in particular DG Regio – provide pro-active guidance in the translation of strategies into action at level of LRAs. It is evident that the closer the administrative tier is ‘to the ground’, i.e. to the everyday life of citizens, the stronger the need for pragmatic approaches. On the other hand there is a need to show a broader variety of options to stakeholders at local and regional level in order to avoid the widespread duplication of similar local policy responses<sup>211</sup>.

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<sup>211</sup> Metis 2011, The complementarity of national and Community interventions aimed at reducing disparities in economic and social development, Commissioned by Committee of the Regions, DTC Unit 4.

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