EU Policies: an Overview

From Decision-Making to Implementation

Dr Rudolf W. Strohmeier and Ingrid Habets (Eds.)

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The Centre for European Studies (CES) is the political foundation and think tank of the European People's Party (EPP), dedicated to the promotion of Christian Democrat, conservative and like-minded political values.
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Profile of the Centre for European Studies

The Centre for European Studies (CES), established in 2007, is the political foundation and think tank of the European People's Party (EPP). The CES embodies a pan-European mindset, promoting Christian Democrat, conservative and like-minded political values. It serves as a framework for national political foundations linked to member parties of the EPP. It currently has 26 member foundations in 20 EU countries. The CES takes part in the preparation of EPP programmes and policy documents. It organises seminars and training on EU policies and on the process of European integration.

The CES also contributes to formulating EU and national public policies. It produces research studies and books, electronic newsletters, policy briefs, and the twice-yearly *European View* journal. Its research activities are divided into six clusters: party structures and EU institutions, economic and social policies, EU foreign policy, environment and energy, values and religion, and new societal challenges. Through its papers, conferences, authors' dinners and website, the CES offers a platform for discussion among experts, politicians, policymakers and the European public.

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Editor's Introduction

Every five years officials of the European Institutions and German Public Representations in Brussels come together to assemble a summary of EU policies. They do so in order to help CDU/CSU's candidates to prepare for the European elections by informing them about the state of play of the EU, the hot topics in Brussels and the policies that are already in place.

These summaries provide useful and concise information for the candidates; the information contained in them is handed to them on a platter, ready to be used in debates and to inform their constituency.

In 2009 the Centre for European Studies (CES), the official think tank of the European People's Party (EPP), decided to produce a volume along these lines in English, for campaigners from all EU countries, and the idea for this book was born.

In view of the next European elections in 2014 the project would be bigger, the summaries would become actual chapters and the readership would be wider. Authors from various Commission departments and German Institutions in Brussels have been invited to write about their fields of expertise. The CES processed and edited the draft chapters into their final versions, which form the core of this book.

Information is central to good decision-making. For a policymaker it is crucial to have up-to-date information and to know the facts in order to convince others of one's ideas. For citizens it is important to form ideas and make choices based on accurate information.

This book does both: it provides useful details, facts and insights for Members of the European Parliament, policymakers and citizens who would like to know more about EU policies. It is not a campaign manifesto, but rather a discussion of a selection of EU policies that have an impact on our lives and our economies.

This book contains 16 chapters on various EU policies, from financial topics to justice issues to foreign policy. It gives a broad and in-depth overview of the EU's and Member States' engagement in aligning issues that concern all of us, across the borders of the Member States. It provides information on the state of play and offers a glimpse of where we are headed. The book is intended for anyone who would like to learn more about EU policies, but especially for policymakers who wish to gain deeper knowledge of specific areas of EU policy.

The European Union affects our daily lives. National governments implement regulations and laws which have been made at the EU level. The EU removes barriers between Member States, and we all profit from the freedom of movement of people and services in the EU. However, it is not always clear how these decisions are made, what policies are in place or the consequences these have for citizens and the EU as a whole. With much ongoing debate about reforming Europe, it is now more important than ever to know more about EU policies.

Abbreviation List

Europe and the Treaty of Lisbon: Origin, Innovations and Future Prospects

CFSP	Common Foreign and Security Policy
ECB	European Central Bank
ECJ	European Court of Justice
EHRC	European Human Rights Convention
EP	European Parliament
MEPs	Members of the European Parliament
SGP	Stability and Growth Pact
TEU	Treaty on European Union (Maastricht Treaty)
TFEU	Treaty on the Functioning of the European Union (Lisbon Treaty)
WTO	World Trade Organisation

The Reform of Economic Governance in the European Union and the Euro Area

AGS	Annual Growth Survey
AMR	Alert Mechanism Report
CAP	corrective action plan
CSR	country-specific recommendations
ECB	European Central Bank
EDP	Excessive Deficit Procedure
EFSF/ ESM	European Financial Stability Facility/European Stability Mechanism
EIP	Excessive Imbalances Procedure
EMU	Economic Monetary Union
ESM	European Stability Mechanism

GDP	gross domestic product
MIP	Macroeconomic Imbalances Procedure
NRP	National Reform Programmes
OMT	Outright Monetary Transactions
RQMV	reverse qualified majority vote
SCP	Stability or Convergence Programmes
SGP	Stability and Growth Pact
SSM	single supervisory mechanism
TFEU	Treaty on the Functioning of the European Union (Lisbon Treaty)
TSCG	Treaty on Stability Coordination and Governance

EU Budget Policy

ALDE	Alliance of Liberals and Democrats for Europe
CAP	Common Agricultural Policy
CFSP	Common Foreign and Security Policy
EPP	European People's Party
EAFRD	Agricultural Fund for Rural Development
ECB	European Central Bank
EIB	European Investment Bank
EP	European Parliament
FTT	Financial Transaction Tax
GNI	Gross National Income
GNP	Gross National Product
IIA	Interinstitutional Agreement
ITER	International Thermonuclear Experimental Reactor, international nuclear fusion research and engineering project
MFF	Multiannual Financial Framework
S&D	Group of the Progressive Alliance of Socialists & Democrats in the European Parliament
SMEs	Small and medium-sized enterprises
SURE	EP Policy Challenges Committee
TEN	Trans-European Networks

TFEU	Treaty on the Functioning of the European Union (Lisbon Treaty)
VAT	Value-added taxes

Taxation Policy in the EU

CCCTB	Common Consolidatd Corportae Tax Base
ECJ	European Court of Justice
ECOFIN	Economic and Financial Council
FTT	Financial Transaction Tax
GJ	Gigajoule
OECD	Organisation for Economic Co-operation and Development
R&D	Research and Development
VAT	Value added tax
TFEU	Treaty on the Functioning of the EU (Lisbon Treaty)

Competition Policy and State Aid Control

ECJ	European Court of Justice
GBER	General Block Exemption Regulation
SMEs	Small and medium-sized enterprises
TEC	Treaty Establishing the European Community (Nice Treaty)
TEU	Treaty on European Union (Maastricht Treaty)
TFEU	Treaty on the Functioning of the EU (Lisbon Treaty)

Enterprise Policy for Small and Medium-Sized Enterprises

CIP	Competiveness and Innovation Framework Programme
COSME	Competiveness of Enterprises and Small and Medium-sized Enterprises
EIB	European Investment Bank
ESF	European Social Fund
EU27	Refers to all Member States of the EU
ERDF	European Regional Development Fund
GBER	General Block Exemption Regulation
IPR	Intellectual Property Rights
JASMINE	Joint Action to Support Microfinance Institutions in Europe

JEREMIE	Joint European Resources for Micro to Medium Enterprises
PPP	Public Private Partnerships
SBA	Small Business Act for Europe
SMEs	Small and medium-sized enterprises

Consumer Protection

CAP	Common Agricultural Policy
EAFRD	Agricultural Fund for Rural Development
ECB	European Central Bank
EEC Treaty	Treaty Establishing the European Economic Community
EPP	European People's Party
FTT	Financial Transaction Tax
GBER	General Block Exemption Regulation
GDP	gross domestic product
GNI	gross national income
GNP	gross national product
IIA	Inter-institutional Agreement
ITER	International Thermonuclear Experimental Reactor, international nuclear fusion research and engineering project
MEPs	Members of the European Parliament
MFF	Multiannual Financial Framework
NCA	National consumer authorities
SEA	Single European Act
SMEs	Small and medium-sized enterprises
SURE	EP Policy Challenges Committee
TEC	Treaty Establishing the European Community (Nice Treaty)
TEU	Treaty on European Union (Maastricht Treaty)
TFEU	Treaty on the Functioning of the EU (Lisbon Treaty)
VAT	Value-added taxes

The Transportation Policy of the EU: The Next Decade

ACDMS	Airport Collaborative Decision-Making System

ATM	Air Traffic Management
CEF	Connecting Europe Facility
EEA	European Economic Area
EGNOS	European Geostationary Navigation Overlay Service
EP	European Parliament
ERMTS	European Railway Traffic Management System
GSA	European GNSS Agency
EGNSS	European Global Navigation Satellite System
ICAO	International Civil Aviation Organization
ILO	International Labour Organization
IMO	International Maritime Organization
ITS	Integrated Transport System
MARPOL ICPPS	International Convention for the Prevention of Pollution from Ships
NAIADES	comprehensive action plan to promote inland waterway transport
RIS	River Information System
SESAR	Single European Sky ATM Research Programme
SOLAS	International Convention for the Safety of Life at Sea
ICSLS	International Convention on the Safety of Life at Sea
TEN-R	Trans-European high-speed Rail Network
TEN-T	Trans-European Transport Network
TFEU	Treaty on the functioning of the EU (Lisbon Treaty)
	Mobilising Justice Policies to Fully Support Growth and Stability in the EU

Mobilising Justice Policies to Fully Support Growth and Stability in the EU

EPP	European People's Party
SMEs	Small and medium-sized enterprises

Research, Innovation and Technology Development Policy

ARTEMIS	Embedded computing systems
ATM	Air Traffic Management

CIP	Competitiveness and Innovation Programme
EIB	European Investment Bank
EIF	European Investment Fund
EIIs	European Industrial Initiatives
EIPs	European Innovation Partnerships
EIT	European Institute of Innovation and Technology
ENIAC	nano-electronics
ERA	European Research Area
ESFRI	European Strategy Forum for Research Infrastructures
FCH	Fuel Cells Hydrogen
FET	Future and Emerging Technologies
FP	Framework Programme
GDP	gross domestic product
ICT	Information and Communications Technology
IMI	Innovative Medicines Initiatives
IPR	Intellectual Property Rights
JRC	Joint Research Centre
KIC	Knowledge and Innovation Communities
OECD	Organisation for Economic Co-operation and Development
PPPs	Public-Private Partnerships
R&D	Research and Development
RSFF	Risk Sharing Finance Facility
SESAR	Single European Sky ATM Research
SET PLAN	European Strategic Energy Technology Plan
SMEs	Small and medium-sized enterprises

Energy Policy at the Centre of European Policy

ACER	Agency for the Cooperation of Energy Regulators
BEMIP	Baltic Energy Market Interconnection Plan
CCS	Carbon capture and storage
EEEF	European Energy Efficiency Fund
EEPR	European Energy Programme for Recovery

ENSREG	European Nuclear Safety Regulators' Group
ENTSO-G	European Network for Transmission System Operators for cross-border collaboration for Gas
ENTSO-E	European Network for Transmission System Operators for cross-border collaboration for Electricity
EURATOM	European Atomic Energy Community
FP6	6th Research Framework Program (2002-06)
FP7	7th Research Framework Program (2007-13)
ITER	International Thermonuclear Experimental Reactor
LNG	Liquid natural gas
TEN-E	Trans-European Network for Energy

European Environmental Policy: Living Well, within the Limits of Our Planet

EAP	Environmental Action Programme
GHG	Greenhouse gas
OECD	Organisation for Economic Co-operation and Development
REACH	Registration, Evaluation, Authorisation and Restriction of Chemical substances

Agricultural and Rural Policy

ACP	African, Caribbean, and Pacific Group of States
CAP	Common Agricultural Policy
GDP	gross domestic product
EAGF	European Agricultural Guarantee Fund
EAFRD	European Agricultural Fund for Rural Development
EAGGF	European Agricultural Guidance and Guarantee Fund
GATT	General Agreement on Trade and Tariffs
LEADER	Links between actions of rural development
LFAs	Less-favoured areas
SAPS	Single Area Payment Scheme
SFP	Single Farm Payment
WTO	World Trade Organisation

European Structural and Cohesion Policy

CEF	Connecting Europe Facility
CF	Cohesion Fund
CoR	Committee of the Regions
CPR	Council Provisions Regulation
DG REGIO	European Commission Directorate-General for Regional and Urban Policy
EAFRD	European Agricultural Fund for Rural Development
EFF	European Fisheries Fund
EGF	European Globalisation Adjustment Fund
EGTC	European Grouping of Territorial Cooperation
EP	European Parliament
ERDF	European Regional Development Fund
ESF	European Social Fund
ETC	European Territorial Cooperation
EUSF	EU Solidarity Fund
GDP	gross domestic product
ICT	information and communication technology
INTERREG	Cross border interregional programs
JEREMIE	Joint European Resources for Micro to medium Enterprises
JESSICA	Joint European Support for Sustainable Investment in City Areas
MFF	Multiannual Financial Framework
NUTS	nomenclature of territorial units for statistics
RCI	EU Regional Competitiveness Index
SMEs	Small and medium-sized enterprises
TEU	Treaty on European Union (Maastricht Treaty)
TEN-T	Trans-European Transport Networks
TFEU	Treaty on the Functioning of the European Union (Lisbon Treaty)
URBAN II	Programme of integrated cooperation in support of urban renewal

The EU's Common Foreign and Security Policy

CFSP	Common Foreign and Security Policy

CSCE	Commission on Security and Cooperation in Europe
EEAS	European External Action Service
EFTA	European Free Trade Association
EUMC	European Military Committee
EUMS	European military staff
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
PSC	Political and Security Committee
WTO	World Trade organisation

The Importance of Development Cooperation for the European Union

AASM	Associated African States and Madagascar
ACP	African, Caribbean, and Pacific Ocean Group of States
CARDS	Community Assistance for Reconstruction and Stabilisation
CDE	Centre for the Development of Enterprise
DCI	Development cooperation instrument
DEVCO	Directorate-General for Development and Cooperation
ECHO	Directorate-General for Humanitarian Aid and Civil Protection
EEAS	European External Action Service
EEC	European Economic Community
EDF	European Development Fund
EIDHR	European Instrument for Democracy and Human Rights
ENPI	European Neighbourhood and Partnership Instrument
EPA	Economic Partnership Agreements
FLEX	system of additional assistance
G7	US, UK, France, Germany, Italy, Canada, and Japan
HIPC	Heavily Indebted Poor Countries
IfS	Instrument for Stability
IMF	International Monetary Fund
IPA	Instrument for Pre-accession Aid
ISPA	Instrument for Structural Policies for Pre-accession
LDC's	Least Developed Countries

MEDA	Mésures d'accompagnement financières et techniques
MDGs	Millennium Development Goals
NGO's	Non-governmental organisations
NIS	New Independent States
NSCI	Nuclear Safety Co-operation Instrument
OCT	Overseas Countries and Territories
ODA	Official Development Assistance
PCD	Policy coherence for development
SAPARD	Special Accession Programme for Agriculture and Regional Development
TACIS	Technical Assistance to the Commonwealth of Independent States
TEU	Treaty on European Union (Maastricht Treaty)
TFEU	Treaty on the Functioning of the European Union (Lisbon Treaty)
WTO	World Trade Organisation

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Europe and the Treaty of Lisbon: Origin, Innovations and Future Prospects

The significance of Europe

The awarding of the Nobel Peace Prize to the European Union in the autumn of 2012 was not only a recognition of the Union's actions for peace; it also underscored the Union's role as an example of regional cooperation. The Nobel Committee not only made clear the historical significance of the European project but also laid out its future orientation.

Europe as a response to globalisation

The EU grew, of course, out of the experience of the horrors of the Second World War, and it is no coincidence that the EU's founders all came from border areas that were the first to have been afflicted by war. The founders included

- Konrad Adenauer from the Rhineland;
- Robert Schuman from Lorraine—he was, after all, born as a German in the empire;
- Joseph Bech from Luxembourg, which was a German stronghold until 1867; and
- Alcide De Gasperi from Trento, which was still part of Austria at the time.

Many of the founders were understandably marked by their war experience—they would later, while dining together at a wine bar in Strasbourg as Members of the European Parliament (MEPs), discover that they had fought on the same section of the front line and had shot at each other. Helmut Kohl also brought up the issue of war and peace from the perspective of his personal experience of the post-war period, even after the

end of his chancellorship. The key question was how war could be made politically impossible on European soil. Jean Monnet found the answer in the communitarian structure of the coal and steel industries, at that time decisive for the outcome of a war, falling back on his personal experiences in those industries before the First World War, when the German coal industry and the French steel industry were linked so as to guarantee the delivery of ore to the French mines as well as the production of the necessary supply of energy for coal mining in the Ruhr region. But these experiences are, of course, ancient history for today's young people.

From a self-critical perspective, however, it should be admitted that the EU—not only Helmut Kohl—clung to this historical European political reasoning for far too long and thus neglected to bring Europe's current foundations to the fore.

The EU's function of providing protection in the face of globalisation has become much clearer. However, the eastward expansion of the EU was exploited by those who were opposed to the globalisation processes that were occurring at the same time, instead of being understood as a response to and a way of addressing globalising trends. A number of issues were, therefore, forgotten:

- Since the middle of the 1990s, productivity growth in the EU has been only half that of the US.

- Over the course of a good 20 years, 250 million farmers in China have abandoned their farms and found employment in factories, working far more than 35 hours a week and far more cheaply than factory workers in Europe. The Chinese economy alone has grown at a rate of about 10% a year for almost 20 years. Thus, Chinese economic output has more than doubled within 10 years. Who, then, buys all these inexpensive 'Made in China' goods—and complains about the loss of jobs in Europe?

- A similar development can be found in India. There are as many engineers graduating there today as in the whole of the EU. Prussia's

ascent as a great European power began 250 years ago with Frederick the Great teaching the Prussian population to read and write during his 40-year reign—and Indian engineers are no less creative than European ones. But some EU Member States have a university dropout rate as high as 40%, and regular education is often no longer provided in deprived areas. Aside from the individuals affected, by allowing such problems to occur, Europe is making major negative investments in itself.

To address these issues—and to draw conclusions from them—is difficult for the Member States not only because of their redistributive reflexes but because the contexts are not sufficiently explained to citizens. Austria is a good example. Before Austria's accession to the EU in 1995, there was an unbelievably intense, professionally run government campaign for accession that was supported by all societal groups. The pro-EU vote of Austrians was overwhelming. There was nothing to follow up, however, even though the next set of challenges was greater: the adjustments connected with accession and the implementation of the Uruguay Round in 1992, with its reduction in trade protectionism after the EU's eastward expansion. The mood today in Austria regarding European politics is among the worst in the EU—and this cannot solely be attributed to the influence of the country's largest newspaper.

Therefore, in the eyes of many—too many—EU citizens, the EU became the catalyst for unbridled globalisation. And it did so at a time when options for national identification had weakened as the result of an unparalleled degree of mobility, plurality and flexibility. At the same time the leeway for economic redistribution, which once cushioned this kind of structural change, no longer existed. But since members of regional or national parliaments prefer to distribute benefits, a third party was needed to state the unpleasant truths, and a frequently prominent Europe was a suitable target. Europe is close enough that it can be railed against convincingly and, at the same time, far enough away that this goes unpunished. It is especially difficult to accept the EU as an unfinished political system, a work in progress, under these circumstances, particularly when citizens' trust in the organisational capacity of politics is declining in general.

But if hiding behind Europe is beneath mature, open-minded citizens and the Lisbon Treaty, as a treaty that brings what happens in Brussels back to the voters, that is, the citizens, then this also means that the Treaty must demand that the citizens become involved with Europe. In that case the citizens, as voters, must grapple with a whole series of issues.

First, they must understand Europe as a partial but concrete response to new worldwide dynamics. The shape of the global economic order in World Trade Organisation (WTO) negotiations, the reorientation of financial market regulations, the significance of an expanded Europe in global trade, the role of Europe as a stabilising force and supporter of peaceful processes of transformation, and the exemplary role of EU integration for economic and political cooperation in other regions of the world, as well as the model of a pluralistic EU are primarily an expression of the EU as an attractive model for others. The undiminished desire for membership also arises from this. But this also shows that the EU acts for national states because an individual Member State—even one of the larger ones—is too small today to be able to assert itself on a global scale.

Such a project must, of course, also be convincing to Europeans in their daily lives. In this respect, one cannot get around the single market, the objectives of Lisbon, the emotional aspects, and the financial and sovereign debt crisis.

A Europe of results

Completion of the single market

Despite a single currency, the single market has not yet been completed—in the view of citizens—in many concrete areas, and EU citizens pay for this with a loss of efficiency. We will find the causes of the loss of prosperity for EU citizens if we look at the still purely national energy markets, the lack of patient mobility based in the national health systems' fear of competition, the anachronistic distribution of frequencies that prevents new business models and the quick closing of blank spots in

Internet access for all, and the closing off of current markets for defence equipment with its prevention of economies of scale.

Today, however, simply citing the abstract economic advantages can no longer justify the intervention of the EU. All parties responsible for European policy—at national or regional political levels—must make clear to the citizen what EU activity means for him or her. This constitutes a Europe of results. Take, for example, the mobile roaming issue, where there was simply no single market for international calls because the competence of the national regulator ended at the border; this fragmentation of power could only be ended in a regulatory way at the EU level. But, as can be seen in the case of the second roaming package[1] with its introduction of price ceilings for international text messages, all national governments fully supported it from the start, although the majority—in contrast to the EP—were opposed to the Commission's proposal of the first package. This was also a positive sign of what the EP could achieve for citizens in collaboration with the Commission.

Europe 2020 strategy

The Lisbon strategy aimed to make the EU a competitive, knowledge-based economic area by 2010.[2] That the ambitious goals of this strategy were not reached in the first decade of the twenty-first century is undisputed. This strategy, however, was not stranded on the effects of the Internet bubble on the world stock exchange or on 9/11 but on the fact that the Member States, especially the large ones, did not trust themselves to implement the adaptations that had been decided in Lisbon. In their follow-up initiative, Europe 2020, which is based on the guidelines Commission President Barroso[3] proposed to the EP for his re-election, the EU sought to avoid precisely those mistakes.

But without binding, positive examples of meaningful EU actions that benefit the citizens, neither trust in the EU nor an emotional bond with EU citizens can be created. Of course, it is possible—to use a witticism of former Commission President Jacques Delors—to argue that just as the single market was not popular, so the Europe 2020 strategy will not be

either. But, as on the national level, politics is successful only when it addresses people's emotions as well as their reason.

The significance of the emotional bond to Europe

Emotions have also been raised in many Member States by the question of Europe's borders, a question connected with the problems of expansion, and not only in countries that border the former Eastern Bloc. The virtual figure of the Polish plumber made an essential contribution to the 'no' of the French referendum.

We could engage in a long discussion as to why it has come to this 'no', and one point can quickly be agreed upon: the consequences associated with the expansion, both positive and negative, were insufficiently communicated to EU citizens or not communicated at all.

Of course, that can be countered with the question of why the EU does not provide more and better information. The Commission would like to do so, but it cannot be done in a comprehensive way with 27 Member States. The Commission's capacity for the task is inadequate and information campaigns, even when they are conducted, are derided as propaganda. But nothing can change if, particularly, the party affliations of MEPs—in Germany for example—are still concealed so that Brussels-bashing by the parties can continue undisturbed.

Another factor here is Turkey's accession to the EU, a topic that never leaves the citizens of Europe indifferent. Whatever the details of an eventual admission, the essential elements of existing EU policies—a common agricultural policy, structural policy and personal freedom—cannot be maintained. To that extent the criteria for EU accession—decided in Copenhagen in 1993 but shoved into a drawer in the meantime—are important.[4] Because EU citizens only vaguely understand the consequences of Turkey's accession, they want information. And why should Turkey, which certainly does represent an interesting market, be able to join but Ukraine not? The citizens discern that the policy has so far not presented a

convincing programme, neither with respect to adaptive capacity nor regarding Europe's borders—and they have reacted negatively.

At present, the question of the debt crisis dominates European citizens' attitudes to the EU. This is true both in the prospering northern Member States such as Germany, where the idea of the exit of Greece from the eurozone is popular without concern for any costs that may result, as well as in the southern Member States, which, having lived beyond their means for years, see the necessary economic measures as dictates, particularly from Germany. It is obvious that solidarity under these circumstances, which directly affect all EU citizens, can be practised only by a reinforcement of integration with clear, enforceable rules.

The increasing plurality of interests and the growing complexity of decisions demand a higher degree of political control. Surveys show that citizens realise that national politics is no longer in a position to answer certain questions satisfactorily. Accordingly, EU citizens are quite prepared to concede a greater role to Europe, at the expense of national governments, in the problems they find important today, such as bank supervision, domestic and foreign security, questions of public health, environmental policy and so on. But the EU has limited competences on these questions. The constitution would have made a great deal of what is demanded of the EU legally possible. In contrast, the Lisbon Treaty is a retreat, but it is, nevertheless, an advance over the status quo, although it must be developed further with respect to a genuine and deeper economic and currency union.

Increasing distance between the Member States and Brussels

Among the most important factors contributing to the inadequate understanding of the European situation, however, are political styles at the EU level that differ from those at the national level. Whoever wants to make politics understandable must first give it recognisable faces. The Lisbon Treaty has taken an important step in the right direction with the appointment of a president of the European Council, the appointment of a high representative and the strengthening of the position of the Commission

president. These changes will contribute to a personalisation of European politics which will be discussed in more detail below.

Even more important is that, as in all Member States, policies be communicated for the most part in transparent political discourse. Nonetheless, on the EU level, such transparency is found only in the European Parliament (EP). Admittedly, this is due to the EP's inherent compulsion towards a larger coalition, for it is only as a large coalition that the EP can impose its will on the Council (and thus the Member States). This is because it is only in the EP that the national and economic conflicts of interest of different stakeholders are settled openly and transparently, particularly because there is no party policy in the political groups. This transparency, however, is still lacking in the Council, as the second arm of the legislature, because even the public negotiations that take place in the minister's councils have mutated into nothing more than a show. As long as the cameras are running, representatives read prepared statements. Actual negotiations and discussions begin only when the cameras have been turned off. The public character of all Council sessions on legislative proceedings, as decreed by the Treaty of Lisbon, has changed little.

If EU citizens would like more transparency in the decision-making processes at European level, and if the implementation of national interests is simply made secondary, then this is possible primarily for the EP, but not for national or regional parliaments, even if national and regional politicians want the voter to believe that it is possible. This is so because both levels can only control the national government in the Council, if they can do even this. Reality shows that only the British House of Commons, the Dutch Upper House and the Danish Parliament control their respective governments in the Council, because these Member States have provided the structures needed to make this technically possible. In Germany, for example, the highest court had to urge the Bundestag repeatedly on this point, for instance regarding its decisions on the Treaty of Lisbon or the euro bailout fund.

The creation of the Treaty of Lisbon

Its origin

On 13 December 2007, in the Portuguese capital of Lisbon, the heads of state and governments of the 27 Member States signed a treaty to reform the EU. This new Treaty of Lisbon represented the results of nine years of steady reform processes. The treaty, a compromise between the interests of the EU Member States, came into effect on 1 December 2009.

The Treaty of Lisbon made numerous improvements to the process of European unification that had been repeatedly demanded by politicians of the European People's Party. These extended from an explanation of the competences of the Union and the strengthening of the principle of subsidiarity (i.e. the recognition of regional and local self-government in preference to the strengthening of the EP and the national parliaments in questions of EU legislation), through to the establishment of the social market economy as the economic system in the EU and to the explicit reference to the value of the Christian concept of humanity in the Preamble, the Charter of Fundamental Rights and the 'church article' of the new treaty.

The EU reform process started with the Treaty of Maastricht in 1991. This created the foundation for an economic and currency union with a stable single European currency. The political union demanded at that time by then German Chancellor Helmut Kohl, of a Europe close to the citizen that was also capable of acting both internally and externally, could not, however, be achieved in Maastricht. The subsequent Treaties of Amsterdam (1997) and Nice (2000) also brought only a few, isolated advances. The parallel, quickly advancing expansion of the EU—from 12 Member States at the time of the Maastricht Treaty to 27 today—therefore increasingly highlights the considerable need for reform of the EU. In retrospect, the EU reform process can be divided into three phases.

The convention phase (1999–2003)

To prepare for the necessary reforms, the heads of state and government held two conventions in succession. The first was the European Convention of 1999–2000 under the chairmanship of Roman Herzog, a former German President and former President of the German Federal Constitutional Court, who was to work on a written fundamental rights catalogue for the EU (as the Federal Constitutional Court had asked him to do in 1974 in its Solange I decision). The second was the Convention on the Future of Europe (the European Convention of 2002–3) under the chairmanship of the former French President Valéry Giscard d'Estaing. It was charged with the task of defining the competences of the EU and its Member States, and the functioning of the EU institutions; making the texts of the European Treaties more efficient and transparent; and strengthening its democratic acceptance and the EU's capacity to act. In distinction from classical diplomatic negotiations, which had determined European treaties for the previous 50 years, both conventions were composed not only of representatives of the governments of the Member States but also included, along with representatives of the European Commission, national parliamentarians (two from each Member State) as well as 16 MEPs.[5] In both conventions parliamentarians were in the clear majority. Moreover, the conventions met publicly, so that their consultations could be followed by every interested citizen. On 2 October 2000, the first European Convention submitted the text it had adopted by consensus for a Charter of Fundamental Rights of the European Union. The Convention on the Future of Europe concluded its work on 10 July 2003 with the Draft Treaty Establishing a Constitution for Europe, also adopted by consensus, which contained the integral Fundamental Rights Charter in its second part.

The government conferences on the Treaty Establishing a Constitution for Europe phase (2003–4)

The conclusion of the work of the Convention on the Future of Europe in July 2003 brought the convention phase to an end. The governments of

the Member States now took over reform negotiations again. In the second half of 2003 and the first half of 2004 a government conference, convened first under the Italian and then the Irish presidency, produced a new treaty text. The government representatives adopted a good 90% of the drafts of the convention. Finally, on 29 October 2004, the Treaty Establishing a Constitution for Europe was signed in Rome. This treaty was intended to put reform of the EU into practice. Although it would be ratified by 18 Member States (by referendum in Spain and Luxembourg, in which the populations voted in favour by 76.7% and 56.5%, respectively), it foundered on 29 May 2005 with the 'no' of the French population (54.7%) and of the Dutch (61.6%) four days later. The Eurobarometer surveys conducted under the auspices of the Commission in June 2005 showed that in France, in addition to internal political reasons, citizens were primarily concerned about unemployment as well as—from the point of view of many—a treaty that was too (economically) liberal and not social enough in orientation. In the Netherlands, the most important reasons for voting 'no' were inadequate information about the treaty, fear of both the loss of national sovereignty and a European 'superstate', and concerns about the costs of Europe as well as general political disillusionment. In any case, the rejection of the treaty in two of the founding states brought the EU reform process to a standstill.

The Treaty of Lisbon phase (2007)

After the Treaty Establishing a Constitution for Europe foundered in 2005, the 18 Member States that had already ratified it primarily occupied themselves with taking up the reform process again. It was only under the German presidency of the Council in the first half of 2007 that a renewed attempt was successful. Of central significance here was the Berlin Declaration, signed in Berlin on 25 March 2007 (the fiftieth anniversary of the signing of the Rome Treaty) by German Chancellor Angela Merkel as President of the EU Council; Hans-Gert Pöttering, President of the EP; and José Manuel Barroso, President of the European Commission, in the presence of the heads of states and governments of all the EU Member States. The Berlin Declaration reinforced the goals of

the EU reform process (more democracy, the strengthening of the protection of fundamental rights and an improved capacity to act for the EU) and ensured that there would be joint efforts up until the European elections in 2009 to put the EU on a new foundation.[6] On this basis, the German presidency of the Council succeeded in negotiating a detailed mandate for the convocation of a renewed government conference, which was resolved on 21–2 June 2007 by the European Council.[7] Here the German presidency of the Council could also count on the support of the new French President Nicolas Sarkozy, who had been elected on 6 May 2007 and had already declared himself open to a simplified treaty. The aim of the renewed government conference was to include in a new treaty as much as possible of the reform content of the Treaty Establishing a Constitution for Europe, while attempting to meet the objections of those Member States that had not yet ratified the Treaty or even (as in the case of France and the Netherlands) had expressly voted against it. Starting with the content of the Treaty Establishing a Constitution, the government conference, which had been meeting under the Portuguese presidency since July 2007, prepared a new treaty that would no longer be described in so highly a symbolic way as a treaty establishing a constitution but instead simply as amending and reforming the existing European treaties. On 29 December 2008, the conference resulted in the signing of the Treaty of Lisbon in the Portuguese capital. In the Preamble to the new treaty the 27 Member States emphasise their common wish 'to *complete* the process started by the Treaty of Amsterdam and by the Treaty of Nice with a view to enhancing the efficiency and democratic legitimacy of the Union and to improving the coherence of its action' (italics added).

But the draft submitted by the EU Commission at the end of November for a deeper, true economic and currency union and the joint paper on that subject by Council President Van Rompuy, Commission President Barroso, President of the Eurogroup Juncker and President of the European Central Bank (ECB) Draghi provided explicitly for an appropriate consolidation of sovereign rights, as well as for responsibility and solidarity on the EU level, which would demand an amendment of the treaty.

The reformed treaty structure for the EU in the Treaty of Lisbon

From a legal point of view, the Treaty of Lisbon, unlike the Treaty Establishing a Constitution, does not re-establish the Union and completely reformulate its foundations in existing treaties. Constitutional language is avoided. Thus, in the Treaty of Lisbon, the Treaty Establishing a Constitution for Europe becomes the Treaty Amending the Treaty on European Union and in the Treaty Establishing the European Community, the Minister of Foreign Affairs becomes the High Representative of the Union for Foreign Affairs and Security Policy, and European law and European framework law again become the well-known guideline or directive. The new treaty also distances itself from the establishment of the symbols of the Union provided for in the Treaty Establishing a Constitution (flag, anthem, Europe day, and so on), which the 16 EU Member States explicitly acknowledged in a declaration annexed to the Final Act of Lisbon. The Charter of Fundamental Rights is no longer integrated into the treaty in full but only by a reference that declares it to be legally binding. Finally, the government conference gave up the mention of the primacy of Union law above national law. In place of that, a declaration also annexed to the Final Act refers to the permanent jurisdiction of the European Community after 1964, according to which European law has primacy of application over national law.

The Treaty of Lisbon adopts about 90% of the content of the Treaty Establishing a Constitution. The treaty incorporates the institutional and substantive reforms confirmed at the government conference in 2007 into the current Treaty on the European Union (the EU Treaty or TEU) and the prior Treaty Establishing the European Community (EC Treaty). The EC Treaty is renamed the Treaty on the Functioning of the European Union (TFEU). This does not, admittedly, lead to a concise, handy constitutional text, as many European federalists had hoped, but to a quite remarkable reorganisation and simplification of European primary law.

In addition, the Treaty of Lisbon clarifies that it is on the amended TEU and EC Treaty—both core treaties of the Union—that the Union 'shall be

founded' and that the two treaties will have 'the same legal value', that is, they equally represent primary law of the EU. Moreover, the Treaty of Lisbon presents a systematic division of the Union's primary law, as had been recommended for some time by scholars, the Commission and the EP, and as had been considered in the Convention on the Future of Europe.

The most important general guidelines for the essence of the EU are attributed by the Treaty of Lisbon to the TEU, which thus becomes the 'general part' of the reformed Union primary law. In this sense the reformed TEU sets the objectives and values of the Union; the relationship between the Union and its Member States and the principles for the delimitation and exercise of Union powers; the fundamental rights to be recognised in the legal system; the democratic principles of the Union, particularly EU citizenship and the role of national parliaments; the organs of the Union as well as its composition, competences and decision-making procedures; the possibility of strengthened collaboration between willing Member States; the general provisions on the foreign actions of the Union, including the common foreign and security policy and the common security and defence policy; treaty revision procedures; the procedures on accession to and withdrawal from the Union; general provisions on the territorial scope of the treaties as well as their duration; and, finally, the official languages of the TEU.

The Treaty of Lisbon devolves to the TFEU the substantive individual provisions on the various political areas of the Union, as well as institutional and detailed procedural regulations on its functioning. The latter thus becomes a special part of the reformed Union primary law. The TFEU, accordingly, contains

- the individual categories and areas of Union competences;
- generally valid provisions for the objectives and principles to be observed in the exercise of its competences;
- the individual provisions on its internal policies and measures for a single market on agricultural and fishing policies;

- provisions for the area of freedom, security and justice;
- economic and currency policies;
- social, environmental, research and industrial policies;
- the specific provisions for foreign activities;
- the procedures for concluding international agreements;
- detailed institutional and financial provisions; and
- general and final provisions.

In addition to the TEU and the TFEU, there are other texts that can be characterised as supplementary Union primary law. Here one finds in particular the (now legally binding) Charter of Fundamental Rights, which was published anew in the Official Journal of the European Union in December 2007, to which the TEU refers and of which it explicitly states in Article 6(1), 'The Charter of Fundamental Rights . . . shall have the same legal value as the Treaties'. Furthermore, the Euratom Treaty is also part of supplementary Union primary law. The text of this treaty, as in the Treaty Establishing a Constitution, was not integrated into the newly composed treaty provisions because of political controversies about the future use of atomic energy, but in line with the first recital in Protocol No. 2 annexed to the Treaty of Lisbon, 'should continue to have full legal effect'.

This comprehensive restructuring of European primary law made possible the landmark decision, which had already been taken in the Convention on the Future of Europe and was confirmed in the Treaty of Lisbon, to grant the EU legal personality and allow it to act legally in place of the European Community. This made it somewhat easier to present European matters both to the citizen and in international relations since a distinction was no longer to be made between the European communities

(which until then had been separate from the EU) and the EU (which previously had not been invested with legal personality).

In legal respects, as well, a great deal was made much simpler through the reorganisation of the treaties—the Treaty of Lisbon signified the end of the complex pillar system of the EU, which since the Treaty of Maastricht had demanded a precise legal and political distinction between political areas under Community law (for instance the single market, competition policy, currency policy and agricultural policy) and fields of activity regulated by Union law (in particular the entire area of home affairs and justice). The coexistence until then of supranational European Community law and Union law (which was to a certain extent under neither parliamentary nor judicial control) was replaced in the Treaty of Lisbon (as already provided for in the Treaty Establishing a Constitution) by one Union law. In the reformed Union law the same organs now issue legal instruments with equal effect according to the same decision-making procedures in all political areas, with some exceptions in the area of Common Foreign and Security Policy (CFSP). The Union organs here are under parliamentary control in the same measure and equally subject to the jurisdiction of Union courts. This is an important structural step in the direction of more transparency and the rule of law in the EU.

The most important reforms in the Treaty of Lisbon

Competence guidelines and monitoring of subsidiarity

The treaty introduces clearly structured guidelines for competences for the first time. In particular, three essential competence categories are defined, namely exclusive competences of the Union, shared competences and, finally, areas for purely supporting, coordinating and supplementary activities. For each of these competence categories the new treaty lists the fields of activity belonging to it, according to the kind of competence. The entire range of competences arises, in addition, in the detailed provisions for every policy, which as a whole were changed little (more on this below).

The 'dispositive competences clause' in Article 308 of the EC Treaty is retained in Article 352 of the TFEU, though in slightly reduced form, because actions by the Union must now take place 'within the framework of the policies defined in the treaties' and require—in addition to the unanimous decision of the representatives of all 27 Member States—the consent of the EP as well. Moreover, the national parliaments retain an explicit right to submit subsidiarity objections against the invocation of this clause. In any event, the time of the extensive use of this clause lies far in the past; it is necessary today mainly in unanticipated crisis situations.

In subsidiarity monitoring the treaty explores innovative avenues. Thus, in the future, national parliaments can introduce subsidiarity objections through an early warning mechanism early in the legislative proceedings directly to the Commission to compel it to reconsider its proposal. Further, they can (like the Committee of the Regions) bring an action against enacted laws or frameworks because they violate the principle of subsidiarity. This right belongs to every single house of national parliament, including, for example, the German Federal Council. With this, the Treaty of Lisbon concedes to the national parliaments for the first time their own place and a direct voice in the institutional structures of the EU. At the same time, it emphasises incomparably more clearly than previous treaties the significance of regions and municipalities. The new treaty recognises explicitly, above all, regional and local self-government (Article 4(2) of the TEU) and also allows the Committee of the Regions to bring subsidiarity actions. Altogether, the Treaty of Lisbon thus brings a definite end to the earlier 'blindness of European law to the regions'.[8]

Reform of EU institutions

A central concern of the Treaty of Lisbon was to reform the functioning of EU institutions so that their efficiency was ensured even after the expansion of the EU to 27 Member States. With respect to the Commission, next to the strengthening of the position of its president by his expanded authority to set guidelines, his right to dismiss commissioners and his election by the EP (see below), the treaty is concerned, above all, with the composition of the

college. In fact, the Treaty of Lisbon provides for a scaled down college as of 2014, whereby the number of commissioners will be equal to two-thirds of the number of Member States, and the Member States are to have a strictly equal rotating right to propose legislation (a system that had been suggested in the Treaty of Nice). According to the concessions agreed upon in Ireland in December 2008, use should be made of an exemption provision in the new treaty so that the Commission can also continue to have one member per Member State after 2014 (see below). The powers of the Commission are not essentially changed in the Treaty of Lisbon but are consolidated and clarified. Points worth mentioning are the expansion of its monopoly on initiatives and its power to start treaty infringement proceedings in the whole area of justice and home affairs, the clarification of its right to represent the EU internationally (with the exception of CFSP), as well as its right to adopt delegated acts. In addition, the position of the president is strengthened because he has the right, among others, to dismiss members of the college, as did in fact happen when Commissioner for Health, John Dalli, resigned over an alleged fraud case.

With respect to the functioning of the Council of the European Union and the European Council, three aspects are dealt with: the Council presidency, the voting arrangements and the expansion of the qualified majority vote. The most important step forward is the expansion of the qualified majority vote (44 new cases). This concerns in particular the area of freedom, security and justice, which includes border controls, asylum, immigration, Eurojust and Europol (on this see below), as well as CFSP, albeit more cautiously. Admittedly, unanimity here still holds in principle, but not if a CFSP act is adopted on the basis of a proposal of the high representative after a request by the European Council. The qualified majority vote is also introduced for some essential aspects of the functioning of the Union, such as comitology and court reform. In contrast, unanimity remains the same in tax law and in social policy.

As of 31 March 2017 another system of qualified majority will be introduced. This rests on the principle of double majority, which will be attained (in general) with the votes of at least 55% of the Member States that

represent 65% of the population. A blocking majority here must represent at least four Member States. This system is completed by the so-called Ioannina mechanism,[9] which makes it possible for a group of states below the stipulated blocking minority to demand a continuation of the debate for a reasonable period of time.

The system of the six-monthly rotation of the presidency is retained for the Council formations that are responsible for internal policies but is abandoned for the European Council and the Council of Ministers of Foreign Affairs. The current president of the European Council or the high representative of the Union will act in place of the rotating presidency in foreign and security policy. This will reduce the importance and visibility of the six-monthly rotating Council presidency of a Member State in the future, but, in exchange, the consistency and importance of EU foreign policy will be strengthened.

The composition of the EP has been reworked in the treaty: the number of seats is limited to 751 (750 plus the president). The share held by each Member State is no longer set down in the treaty but in an act of the European Council on the proposal of the Parliament, which must follow the principle of degressive proportionality with a minimum threshold of 6 MEPs and a maximum of 96. These rules were not able to be applied during the European election in June 2009. The EP was thus elected in accordance with the Treaty of Nice (736 seats, of which 99 were reserved for Germany). But, in line with the resolutions of the European Council of December 2008, a protocol for temporarily amending the treaty was introduced in 2010, in accordance with which 18 MEPs were still nominated for the current legislative period 2009–14.

Reinforcing the principle of democracy

Strengthening the EP

The Treaty of Lisbon reinforces the democratic legitimacy of the EU in multiple respects. In the first place, there is the strengthening of the EP, making a leap unprecedented in its history. It becomes a co-legislator in

almost all political fields. Newly added are more than 30 individual areas, including core policy areas such as agriculture, justice and home affairs (asylum, immigration policy and criminal law), structural funds and the Cohesion Fund, and trade legislation, as well as reform of the EU's jurisdiction. Only where the Council still acts unanimously can it adopt laws after merely consulting the EP.

In budgetary procedures the EP now has a strictly equal position with that of the Council. The distinction between obligatory and non-obligatory expenditures—in the former, particularly in agricultural policy, the Council had the final say until now—has been dropped.

International agreements of the EU need, as a rule, the consent of the EP if the subject areas involved are those for which internal legislative proceedings apply. This is an enormous expansion over the previous treaty and will lead to the obligation to endorse all meaningful agreements, including those in the WTO area.

With the introduction of the delegated acts, the implementation arrangements are adopted on the EU level by the Commission according to procedure, which grants equal right of control to the EP with the Council.

The EP elects the Commission president on the basis of a proposal that the European Council makes with a qualified majority. Here the balance shifts more towards the EP. What counts is not only that the act of Parliament is now qualified as an election and not as an approval of the nomination by the European Council. Also, the Council proposes its candidate after taking into account the elections to the European Parliament and this proposal has to find an absolute majority in the EP (see Article 17(7) of the TEU).

The democratic legitimisation of the EU does not depend only on the position of the EP. Other innovations in the draft Convention contribute decisively to strengthening it, such as, for instance, the augmentation of the role of national parliaments in the decision-making procedures of the EU,

especially the direct involvement of the national parliaments in monitoring subsidiarity (see above). It also introduces the rule that the meetings of the Council as legislator are to be public.

Greater monitoring of subsidiarity in the Treaty of Lisbon

In a material sense, the Treaty of Lisbon proposes only a small yet not unimportant clarification of the definition of the principle of subsidiarity: according to the new wording of the article, both criteria (insufficient achievement of goals by the Member States, better achievement of goals by the EU) must be met in a clearly cumulative way. The requirement of the true added value of the Union level thus cannot simply be assumed, as is apparent in the current treaty provision (see Article 5 of the TFEU: 'but more' instead of 'and . . . therefore' as previously in Article 5 of the EC Treaty).

But the Treaty of Lisbon favours strengthened monitoring of political subsidiarity. This is established in an entirely new early warning mechanism for use by the national parliaments, which is arranged in a new subsidiarity protocol that replaces the current protocol of the Treaty of Amsterdam. This mechanism runs as follows:

- A national parliament or house of a national parliament may, within eight weeks of the transmission of a draft legislative act, explain in a reasoned opinion to the Commission, Council and the EP why it holds that the draft does not comply with the principle of subsidiarity.

- Every national parliament has two votes: in the case of a bicameral system, each house has one. In any case the Commission, Council and the EP have to consider the reasoned opinions, regardless of the number of votes.

- If reasoned opinions are issued by parliaments with at least one-third of all the votes, the Commission must review its draft and give reasons for its decision (withdrawal, amendment or maintaining).

- If reasoned opinions are issued with at least half of the votes and the Commission maintains the draft nonetheless, the legislative procedure can be stopped by a specific resolution of the Council (with a 55% majority of the states) or the EP (with an absolute majority).

Another new point in the Treaty of Lisbon will strengthen the monitoring of political subsidiarity in practice as well, namely, the principle of openness in the Council: all consultations and voting in the Council on legislative acts are, in the future, to occur in open session. The increased transparency that results will help the general public, as well as national parliaments, regions and organisations, to follow the acts of the respective ministers in the Council, including on issues of subsidiarity.

Also, the reduction of the number of Commission members in the Treaty of Lisbon to two-thirds of the number of Member States would be more conducive to solidarity than a large Commission in which 27 or more portfolios need to be created. According to the concessions to Ireland agreed upon in December 2008, use should be made of an exemption provision in the new treaty so that the Commission could also continue to have one member per Member State after 2014.

Finally, the new subsidiarity protocol enables the national parliaments or any house of those parliaments to bring a new subsidiarity action before the European Court of Justice (ECJ) subject to the respective national legal system. Such actions should certainly, in any case, come from Germany. Moreover, a similar right to bring an action is granted to the Committee of the Regions. Because the principle of subsidiarity is justiciable in only a limited way, the actual significance of the new protocol depends on whether the ECJ will extend its purview to actions concerning the overstepping of competences. Despite the careful wording of the protocol, this is not excluded, for adherence to the competences of the EU is logically prior to the principle of subsidiarity, and judicial control is also more easily accessible.

Already in May 2006 the Commission had decided on the initiative of its president to forward all its proposals directly to the national parliaments and

to give them the opportunity to submit a reasoned opinion on, among other things, subsidiarity and proportionality (the 'Barroso procedure'). This initiative was well received by the national parliaments and represents a partial anticipation of the new mechanism for monitoring subsidiarity in the Treaty Establishing a Constitution for Europe, which was once again reinforced in the Treaty of Lisbon.

Practically speaking, the most important innovation in recent years has been the explicitly elaborate impact assessment system of the Commission, the central part of its agenda for better regulation. Primarily through the high level Impact Assessment Board set up in 2006 in the Commission, the examination in its entirety of the impact of the regulation proposals being drafted is much more efficiently ensured. This will also lead directly to subsidiarity problems becoming better known in the Commission and being critically assessed. At the beginning of 2010, the standing of this board was increased by President Barroso in that he granted it a de facto right of veto in the departments' internal voting process with respect to insufficient impact assessments. A continuing problem is that the Council and the EP, even if they do not yet discuss changes, however sweeping, to the Commission proposal, cannot carry out any impact assessment on their own, although this has long been required by the Commission.

With these regulations, especially the political early warning mechanism, in the hands of national parliaments, the Treaty of Lisbon can lead to stronger monitoring of subsidiarity if the national parliaments make use of the mechanism. They will need to be efficiently organised to process the legislative proposals of the Commission quickly and also to be able to vote with other national parliaments. Because the Commission's proposals do not come out of the blue but are based mostly on public consultations, this is entirely possible. For the rest, the national parliaments in the Conference of Community and European Affairs Committees of the Parliaments of the European Union (on the basis of the Barroso Procedure) have already begun to coordinate their monitoring. Even if it is likely within the framework of the early warning mechanism that the formal quorum of a third or even a majority would seldom result in negative reasoned opinions, the mere

existence of the mechanism, like that of the right to bring an action, will further strengthen the importance of subsidiarity issues.

In any case, the regulations made are clearly superior to the alternatives discussed in the Convention on the Future of Europe. Both a special (administrative or political) subsidiarity monitoring organ on the EU level, and its own court of competence staffed with national and European constitutional judges, were rightly rejected. The former idea represented the structure of a wider EU bureaucracy, whose political importance would be less striking because of its special task than the reasoned opinions of national parliaments. A court of competence of its own, alongside the ECJ, would be completely impractical. The monitoring of the legal foundations of the EC Treaty cannot be separated from the other interpretations of Community law, and the establishment of a second European court would not lead to different thinking on European law than in the ECJ, whose judges also come from the Member States and are not appointed by EU organs.

Fundamental rights and the protection of rights

The Treaty of Lisbon made the Charter of Fundamental Rights legally binding. Here are some of the principles necessary to understand it:

- The Charter presupposes the current level of protection of the European Convention on Human Rights (ECHR) but goes beyond it in various respects and adds fundamental rights that were still completely unknown in 1950, for instance, the prohibition of the reproductive cloning of human beings (Article 3(2)).

- Like the catalogue of fundamental rights in the German Constitution, the Charter cites the inviolability of human dignity in Article 1 and thus shows from the beginning its value orientation and the Christian concept of humanity behind it.

- The Charter includes only citizens' and human rights and does not in any way create new EU competences; in principle, it should not be invoked for an expanded interpretation of existing responsibilities.

- In principle, the Charter is binding on the Union organs and on the Member States only 'when they are implementing Union law' (Art. 51 (1)). The UK and Poland have also declared in a protocol that they have certain reservations but must view the fundamental rights in their entirety as general legal principles of EU law.

Furthermore, the treaty provides for the EU itself joining the ECHR. This is to appreciate that the citizens of the Union retain the same protection from the Union organs through the Strasbourg Court as they have always enjoyed from the Member States.

In addition, several protection provisions are included that were heavily criticised in the past. Above all, the general regulations on judicial monitoring by the ECJ were also extended over the area of justice and home affairs, in particular what was until then the third pillar, including Europol's activities. At the same time, the right of private individuals to bring an action to the ECJ, a right that often was criticised as too restrictive, was relaxed somewhat.

Association with values and religion

The EU's adherence to values and the significance of religion are considerably more clearly expressed in the new treaty than previously. Thus the Preamble to the TEU now refers to the 'cultural, religious and humanist inheritance of Europe' from which the EU 'draws inspiration'. The essential values and objectives of the Union are better expressed in the Treaty of Lisbon. The new Article 2 of the TEU holds to the following values: human dignity, freedom, democracy, equality, rule of law, the observance of human

rights, pluralism, non-discrimination, tolerance, justice, solidarity and equality between men and women. Among the objectives of the Union in Article 3, those of peace, a competitive social market economy, sustainable development, cultural plurality, solidarity, social cohesion, and free and fair trade are highlighted. Finally, it is remarkable that an article on churches has been added. This article converts into a rule of primary law the currently non-binding guarantee of the place of churches and religious as well as non-confessional organisations.

Establishing the social market economy as the economic system of the EU

According to Article 3(3) of the TEU, the EU was to work in the future on 'a highly competitive social market economy, aiming at full employment and social progress'. This regulatory postulate by Alfred Müller-Armack and Ludwig Erhard, which is law in the German Federal Republic, has the status of economic constitutional law for the EU and its 27 Member States. The Treaty of Lisbon adds other principles of economic constitutional law that are borrowed from German thinking: the priority of price stability and therewith combating inflation for currency policy; the strong independence of the ECB as an institutional safeguarding of price stability; the requirement of healthy public finances; and the principle of competition that, despite French attempts to remove it from the new treaty, is still an important part of European treaties. A European economic government equipped with economic, tax and socio-political competences and a strong budget is not part of the Treaty of Lisbon. Instead, economic, tax and social policy continue to be broad national competences, even if the need for coordination has risen sharply in a market that is becoming ever more integrated, especially in view of the debt crisis in the states. For that reason the existing frameworks of the treaty are now being used more widely to promote powerful economic governance.

Specific policy areas

Foreign and security policy

The Treaty of Lisbon is intended to strengthen the activities of the Union as a real force on the world stage. The office of the High Representative for Foreign and Security Policy serves this purpose primarily, combining the three functions of a vice-president of the Commission, commissioner for foreign policy and the chairman of the Council formation for foreign affairs, and that of the previous high representative for CFSP in one individual to whom the European External Action Service is answerable. The creation of the single legal personality of the Union, which puts an end to the present confusion between the European Community and the EU, will also essentially help the Union to assert itself better on the international stage.

The intergovernmental features of the actual CFSP are widely retained, including the reduced role of the EP and the ECJ, and the decision-making process in the Council. Thus, in principle, the rule of unanimity still applies, to which there is, however, an interesting exception: proposals by the High Representative after a request by the European Council. In the area of security and defence policy the treaty sets new forms of closer collaboration between individual willing Member States, culminating in the recognition of a mutual assistance obligation.

What merits consideration in the area of the common Europeanised external relations of the Union is that the treaty qualifies the common commercial policy as the sole competence of the Union and at the same time introduces in principle the normal common decision-making process, the qualified majority and co-decision or consent of the EP. But the sole competence, which avoids having to ratify agreements by the 27 Member States, also only holds for external relations. Commercial agreements in the area of culture, for example, do not lead to an unwanted ‘shifting’ of competences in internal relations between Member States and the EU.

Freedom, security and justice (asylum, immigration, civil and criminal law)

Further ahead still of foreign policy is the policy area in which the Treaty of Lisbon brings the clearest advance in integration. It provides the de facto communitisation of the third pillar, thus police and judicial collaboration in criminal matters. Accordingly, as in all other areas, regulations and directives will in future be proposed by the Commission and approved jointly by the EP and the Council. In principle, the latter acts with a qualified majority (not in questions of operational police collaboration and only to some extent in the harmonisation of criminal law). The ECJ will be able (after a transition period of five years) to grant almost full legal protection and can also be called on by the Commission in treaty infringement proceedings. The Commission enacts the necessary implementation provisions on the Union level and negotiates international agreements.

The price for this true quantum leap was the expansion of the opt-out possibility for the UK, Ireland and Denmark in the entire area of justice and home affairs. It still ended in a complete reformulation of the legal foundations of police and judicial collaboration in criminal cases to make them considerably more precise than the vague previous provisions in the TEU that ultimately allowed everything. The transition to majority decisions and the more efficient instruments of the Community presuppose that the new Treaty focuses on core areas in which European activity is truly required.

In the already communitised area of domestic policy (asylum, immigration and border controls) the Treaty sets ambitious goals that had, however, been agreed upon politically for some time by the European Council. It also makes the ordinary legislative procedure applicable, thus the qualified majority in the Council and co-decision with the EP. This also holds for the creation of a European asylum system and an integrated external border security system. For immigration policy, the transition to a qualified majority, as in criminal law, in return for a clear delimitation of competences (added at German urging) was reached. The Member States are only

responsible for determining how many third country nationals looking for work may enter.

Other Policy Areas

Other policy areas have been changed only on very isolated points. In particular, the competences and decision-making mechanism in the areas of the economy and social affairs remain virtually unchanged. Here are a few examples of isolated changes:

- *Energy*. A new unified legal basis is provided for, by which measures can be implemented regarding the functioning of the energy market, the security of the energy supply, energy efficiency and the development of renewable energy as well as the connecting of energy grids. Further, a clear reference is inserted to the solidarity between the Member States in the area of energy. Expansions of competences here are hardly opposed to the present legal basis, but the coherence and efficiency of this policy, which has become central, has been increased.

- *Economic and Currency Union*. In procedures for monitoring budgetary discipline, the Commission can in future issue a first warning to a Member State. Further procedures remain what they were before. For the rest, the Member States belonging to the eurozone (16 when the procedure was initiated) can decide in the Council itself, that is without the voting rights of other states, on special measures for the monitoring of their budgetary discipline and on guidelines for their economic policy, irrespective of general sanction procedures and the guidelines adopted for the EU as a whole. This new legal basis (Article 136 of the TFEU), previously ignored for the most part, has proven to be an indispensable basis for the legislative package for strengthening the Stability and Growth Pact (SGP); it increased effectiveness as it provided for implementing previous radical sanctions against euro states where there had been excessive budget deficits or a lack of action to counter dangerous macroeconomic inequalities.

- *Services of general economic interest*. A new protocol defines the general value of these services. Further, a new legal basis would make it possible to determine the principles and conditions for its functioning (within narrow limits).

- *Space*. The introduction of a new legal basis by which the Union can introduce a European space policy, including a European space programme.

The treaty contains other marginally new competences for the support of tourism, sports and civil protection.

Outlook

Dealing with the financial and debt crisis

The euro has already been briefly mentioned. The heads of government decided at the 2008 December Council that the economic recovery plan of €5 billion was not of decisive significance from a purely budgetary perspective.[10] Much more important was that the EU Commission was able to force through the strengthening of the SGP and enforce both the substance as well as the monitoring of the EU economy as a result of the faster decisions for state aid, which is the basic condition for a single market. That several Member States already had the axe in their hands should not be especially emphasised. In the meantime the EU, as the EP had long demanded, had approved far-reaching legislation for regulating and monitoring the financial markets (see the chapter on economic governance for more on this).

A new, yet much more serious challenge to the credibility of the EU was the arrival of the debt crisis caused by Greece in early 2010 that, given the almost irrational reactions of the markets, seemed to threaten even the existence of the euro. This danger was averted by determined action on the

part of the EU organs and the states of the eurozone. Provisional stability mechanisms—that is, a bailout fund—were created to give financial help under strict conditions to euro states in dire straits. So that such a stability mechanism could also be made permanent and legally unassailable after 2013, it was decided by the European Council in March 2011, exclusively at the wish of the German government, to simplify a clarifying change in the treaty. At the same time, as of the summer and autumn of 2010, the Commission introduced a far-reaching legislative sharpening of the Stability and Growth Pact, as well as a radical reform of the economic coordination within the framework of the European Semester, in order to ensure that the finances of any single Member State, and particularly those in the eurozone, would not get out of control again. The first European Semester was successfully implemented in the first half of 2011.

On the relativisation of the subsidiarity problems in current practice

A glance at the political reality shows that subsidiarity problems arise relatively seldom. This has to do, first, with the fact that the total number of European Community acts accepted annually in comparison with the peak times of the production of European Community regulations (such as during the time of the Delors Commission) is clearly diminishing. But above all, 15 years after its introduction, the subsidiarity principle has been largely internalised among the politicians and officials in the organs and Member States. Even in the Commission's preparatory work, ideas inimical to the idea of subsidiarity were for the most part ruled out by the General Secretariat, the Legal Service or other departments or on the political level, without this coming out. The reformed impact assessment system and its board will do everything it can.

For that matter, subsidiarity is a dynamic concept, the assessment of which changes naturally over the course of time. Changed circumstances today require action on the European level in areas that a few years ago would be left even more to the Member States, for example, energy policy and climate change; and regulations concerning, and supervision of, justice, home affairs and (completely current) financial markets, as was necessary

for the euro bailout. Conversely, within the area of EU social legislation, a discernible deceleration in comparison to the 1980s and 1990s has occurred. By and large, it can hardly be disputed that the current legislative priority of the EU reveals the great challenges of the time, such as globalisation; the financial, economic and currency crises; energy security; and climate change. These challenges today require more European legislation than could have been expected five years ago. The question connected with this is whether, parallel to that, the return of competences to the Member States—as various national parliaments have demanded—should not also be considered so that there is increased acceptance of EU legislation.

Also undergoing change is the choice between the instruments of regulation or directive (actually a question of proportionality). If the preference for directives was so popular in the 1990s that it was highlighted in the protocol on subsidiarity in the Treaty of Amsterdam, the pendulum has now swung in the other direction. Today there is often a preference for regulation expressed—without any complaint on the part of the Member States—in order, for instance, to be able to respond more quickly to the financial crisis (for example, the regulation on rating agencies) or to avoid bureaucracy in connection with monitoring the implementation of legislation in protracted treaty infringement proceedings.

Typical difficulties in dealing with subsidiarity issues

In the few true problem cases some typical difficulties in dealing with subsidiarity issues can be seen, which should be brought to light in the interests of a genuine political debate.

First, the administrative support of Member States can vary a great deal. Many problems that from a German or French perspective, for example, could continue to be left without difficulty to German states or a professional centralised public service are viewed entirely differently in certain other Member States. There, Community regulations first make it possible to also demand a more effective administration of treaty infringement and other

monitoring proceedings. This should be considered in discussions on, for example, environmental policy—on soil protection, for instance.

Second, subsidiarity is a matter of opinion. The assessment of subsidiarity often ends up being very subjective and depends on different national experiences, backgrounds and interests. For example, the German problem with anti-discrimination directives is not understood at all in many other Member States. This could have something to do with cultural assumptions that are different in Scandinavia or in the Romance countries but is also related to a special German legal tradition, in which treaty autonomy is more highly valued than elsewhere. Or, to cite a different example, if the Commission repealed the norms for the quality of fruit and vegetables (the curvature of cucumbers and so on), thus eliminating one of the classic criticisms of subsidiarity, it would then have to support subsidiarity issues against the tangible interests of industry.

Third, subsidiarity can be unpopular. Every now and then it amounts to rather symbolic legislative acts, in which reasoned subsidiarity objections are deliberately put aside in view of the high sympathy value that the principle has for the EU. Examples are the EU ban on importing dog and cat fur (which was actually of minimal economic significance), and the provision of food aid by the European Community to the needy (as a consequence of the reform of the Common Agricultural Policy, the giving of food aid is not really possible from intervention stores, so it was proposed to give it as EU financial assistance for the procurement of foodstuffs in the market). For the rest, the initiatives mentioned here are in no way inventions of the Commission but demands by the Member States and the EP.

Transnational civil society and European identity

According to Wolfgang Schmale, the EU came into being against the background of European history as a construct of political reason, carved out by an elite of politicians, scientists, journalists and intellectuals.[11] Demands for European unification, however, could already be found in the objectives of large parts of the European resistance to Hitler's Germany, and it can therefore

hardly be classified as a purely elite project. But Schmale does correctly emphasise that the number of themes that establish a European public is steadily increasing. The circle of the actors is increasing rapidly in tandem. It includes not only the 'classical Europeans', who work in the institutions, or the lobbyists, representatives of civil society, scientists and journalists who are closely connected with Brussels and Strasbourg, but also includes all those involved in one of the many EU projects through research or regional politics, for example. Today all of these individuals amount to one million people who constitute a comprehensive European demos. This is more heterogeneous than a national state, even if one considers the social changes resulting from immigration, but the necessary coherence should be obtained through the communications links institutionalised in the EU system. Schmale therefore speaks of the 'coherence in diversity' by which he summarises this current European identity.

European identity cannot, should not and will not replace national and regional identity. Rather, these identities represent concentric circles that are not mutually exclusive but individually overlap and supplement each other in various ways. This is already true for those who live in border areas—previously because they had to change their nationality time and again as borders shifted, today because one's neighbours across the border sometimes appear to be at least as familiar as one's own compatriots.

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[7] European Council, 'Conclusions, 21–22 June 2007', CONCL 2 (20 July 2007), accessed at http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ec/94932.pdf on 22 March 2013.
[8] W. Frenz, *Handbuch Europarecht*, vol. 6 (Heidelberg: Springer, 2011), 645.
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Dr Markus Schulte

The Reform of Economic Governance in the European Union and the Euro Area

Introduction

The term 'EU economic governance' in its broadest sense denotes the totality of the rules, procedures and institutions determining the economic and financial policies conducted in the European Union, based on the provisions of the Treaty on the Functioning of the European Union (TFEU).[1] In this chapter, after discussing broad lessons learned in the context of the financial, economic and sovereign debt crises, we concentrate exclusively on recent and ongoing reforms to economic policy coordination. These include the reform of the Stability and Growth Pact (SGP) and the creation of the procedure for preventing and correcting macroeconomic imbalances, as well as additional legislative proposals under discussion (the 'Two Pack') and the Treaty on Stability, Coordination and Governance in the Economic Monetary Union (EMU). The chapter concludes with a short sketch of the state of play as of February 2013 regarding the discussion on completing EMU. While desirable in terms of gaining a complete picture, it is not possible in the context of this brief chapter to fully reflect on the creation of mechanisms for providing financial assistance to euro area Member States. Nor will the steps already taken since 2009 to enhance financial sector supervision by creating the European System of Financial Supervision or the more recent proposals made to move towards a single supervisory mechanism and eventually towards full banking union be covered in any detail. However, reference is made to these issues in the analysis of the lessons learned in the context of the crisis, as well as in the discussion of the state of play in the concluding section. EU economic governance has been evolving rapidly and significantly since the financial crisis erupted in 2007/8 and is likely to continue to evolve over the coming years. Because of this, the present chapter can only provide a snapshot of the state of play at the beginning of 2013.

Lessons learned in the context of the financial, economic and sovereign debt crises

The global financial crisis that erupted in the United States in 2007–8, the 'great recession' that followed in 2009, and the sovereign debt crisis in several euro area Member States that ensued in 2010 revealed weaknesses in the economic governance of the European Union and the euro area. While these weaknesses were not causes of the successive crises, they contributed significantly to increasing the degree of vulnerability of the EU, and in particular of the euro area, to the various shocks associated with them. The lessons learned in the context of these crises led to legislative and non-legislative initiatives from the Commission in order to address the weaknesses that had been identified. It also led to the creation by euro area Member States of intergovernmental arrangements for the provision of financial assistance and the conclusion of an intergovernmental treaty containing, *inter alia*, the 'Fiscal Compact'. The difficulty in swiftly finding a fully convincing solution to the sovereign debt crisis in the euro area, the formation of negative feedback loops between weaknesses in banks' balance-sheets, doubts about sovereign debt sustainability in some countries and the poor growth outlook combined to bring about a dangerous crisis of confidence in which the very existence of the euro was called into question. In response, a significant further deepening of EMU has been under consideration by the European Council since June 2012, including steps to create more integrated frameworks for financial, budgetary and economic policy, as well as to ensure their democratic legitimacy and accountability.[2]

Developments in the run-up to the crisis

An analysis of pre-crisis economic and financial developments reveals that many of the problems that the EU has been facing in managing and overcoming the successive crises had, in good part, already built up long beforehand. In public finances, the relatively good economic times prior to 2008 had not been used to reduce budget deficits and levels of public debt in

terms of gross domestic product (GDP) to any significant extent. Some Member States (e.g. Belgium, Greece and Italy) had, before the crisis, already built up debt levels very significantly above the 60% threshold in terms of GDP set by the Maastricht Treaty, rendering them more vulnerable when revenues dropped in the wake of the slump in economic activity in 2009.

For other Member States (in particular Ireland and Spain) with a previously fairly good fiscal policy record, the crisis brought about a very considerable expansion in the level of public debt. This was mostly due to macroeconomic imbalances, such as housing bubbles and associated financial sector vulnerabilities, as well as an erosion of competitiveness that had been building for years prior to the crisis. With the construction and financial sectors having been major growth-drivers while the bubble was building, when it burst it meant that associated tax revenue windfalls suddenly dried up, while expenditure could not be adjusted quickly enough. Deficits therefore ballooned and debt levels increased rapidly. In addition, where the bursting of the bubble also immediately threatened the stability of the banking system (as was the case in Ireland), significant public funds needed to be committed to rescuing the banks. In this way, Ireland's debt level more than quadrupled between 2007 and 2010, while Spain's almost doubled during that period and has risen further since.

Another significant pre-crisis development that had a bearing on post-crisis adjustment burdens was the sizeable divergence in Member States' competitiveness, particularly within the euro area, as reflected in large differences in the evolution of real effective exchange rates and persistent current account deficits in some countries, as well as similarly persistent surpluses in others. This development is indicative of an insufficient adjustment capacity in some euro area economies. Such a capacity, in particular the flexibility of product and labour markets, is essential for the successful operation of a monetary union, where the nominal exchange rate is no longer available to bring about adjustments in competitiveness. Put simply, where the rate of wage inflation persistently exceeds the rate of productivity growth, prices will rise and competitiveness vis-à-vis other euro area economies with more balanced wage and price inflation will be eroded.

Finally, the EU, and particularly the euro area, has long been underperforming vis-à-vis comparable economies (e.g. the US) in terms of economic growth and productivity, suggesting that the structural reform agenda pursued in the context of the Lisbon strategy has not yielded sufficient results.

Weaknesses in economic surveillance

While responsibility for the adverse pre-crisis developments sketched out above lies chiefly with the Member States concerned, there is no doubt that weaknesses in the surveillance arrangements underpinning the coordination of Member States' economic policies have also been a factor in producing these outcomes. The crisis itself has demonstrated very clearly that economic and financial developments in one Member State can very significantly affect those in other Member States (the spillover effect). The presence of such an effect is the very rationale for the coordination of economic policy as set out in Article 121 of the TFEU, which stipulates that EU Member States have to regard their economic policy as a matter of common concern. Surveillance of Member States' economic policy on the basis of the Integrated Guidelines, which consist of the Broad Economic Policy Guidelines (Art. 121 TFEU) and the Employment Guidelines (Art. 148 TFEU), as well as SGP, should have, but has not, ensured that fiscal deficits were reduced during economic good times and that public debt either remained below or was brought down to the 60% of GDP threshold at a satisfactory pace. Among the reasons for the failure to achieve this was the fact that the incentives for compliance with the rules provided by the SGP were not large enough, that it was relatively easy to organise a blocking minority within the Council against warnings or sanctions proposed by the Commission, and that the option of imposing sanctions came too late in the process to have any dissuasive effect. In fact, the option of sanctions had never been used in the past under the SGP. Also, while the 60% debt criterion was enshrined in the Maastricht Treaty, it had no significant operational role in the application of the SGP as it was assumed that strict observation of the 3% deficit criterion would quasi-automatically also ensure compliance with the debt criterion.

Another important weakness of the pre-crisis surveillance arrangements was their 'blind spot' for macroeconomic imbalances and

competitiveness developments. While such developments were analysed in the context of the Commission's reports on Member States, and in particular in the euro area's informal biennial competitiveness reviews, there was no formal instrument for their systematic analysis and follow-up through concrete policy recommendations. In addition, the mechanisms for fiscal policy surveillance and the surveillance of economic and employment policies were not aligned, leading to a somewhat fragmented rather than fully integrated approach to policy analysis and policy guidance. Finally, when policy advice was given to Member States in the form of Opinions on Member States' Stability or Convergence Programmes (fiscal policy) and country-specific recommendations (CSRs, economic and employment policies), it tended to be at different points in time during the year and for the most part came only after key national policy decisions had already been taken, that is, *ex post* rather than *ex ante*. This limited the effectiveness of EU and euro area policy guidance in the formulation of national economic policy.

An insufficient institutional set-up for the EMU[3]

Beyond the lessons learned regarding weaknesses in the field of economic policy coordination—whose ultimate purpose is the prevention of crises—the financial crisis and the sovereign debt crisis in some countries in the euro area also highlighted the fact that the institutional set-up for EMU, as put in place by the Maastricht Treaty, was also insufficient for the efficient management and resolution of crises. The financial crisis in 2008 had already demonstrated that very close coordination between Member States, and particularly their authorities for banking supervision and regulation, was essential if a meltdown of the EU's financial sector was to be averted. What had long been postulated by academics and some policymakers became fully evident during the financial crisis: the existence of a closely interconnected single market for financial services without a single supervisory regime overseeing it made the management of the banking crisis much more difficult and much more costly for the taxpayer than would otherwise have been the case.

The absence of an instrument to provide financial assistance to the Member States of the euro area became a problem in May 2010, when it became evident that Greece would no longer be able to roll-over its debt and would most probably face a disorderly default unless financial assistance could be provided. It is not entirely clear whether the absence of such an instrument was mainly a deliberate choice of the creators of the EMU, with the objective of preventing moral hazard, that is, incentives for some to have a free ride at the cost of others. While this probably played an important role, it might also have been the case that the relative stability in the EU's financial sector in the recent past had led policymakers to believe that such crisis situations were unlikely or that the preventive instruments of economic policy coordination would suffice to avert them. Regardless of the reasons, the massive economic, social and political costs associated with a potential sovereign default of one or more euro area countries made it clear to policymakers that such an instrument was indeed needed.

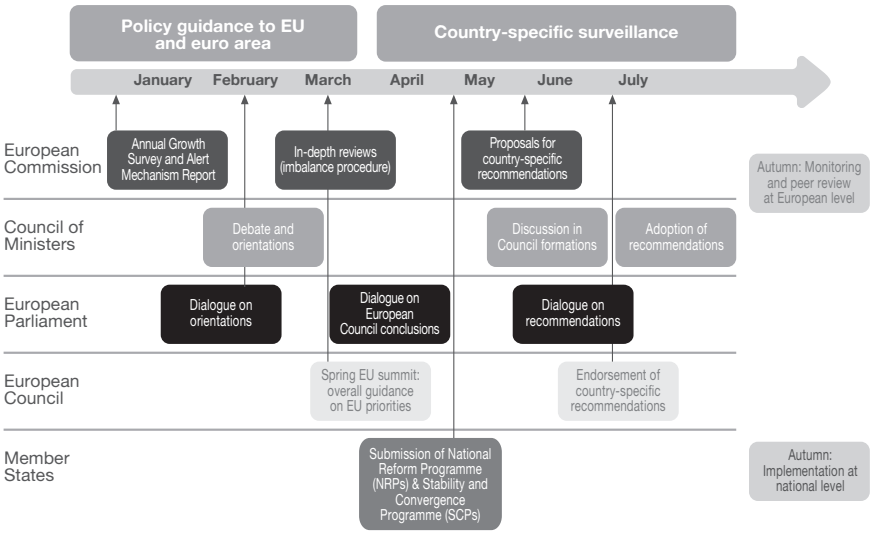
Reforming economic policy coordination: integrated surveillance

The European Semester

The introduction of the European Semester in 2011 was the first step towards correcting some of the weaknesses of economic policy coordination identified in the context of the crisis. The term 'European Semester' refers to the first six months of the year during which 1) the identification of the EU's, the euro area's and Member States' main economic challenges; 2) the analysis of their respective policy performance; and 3) the presentation and adoption of recommendations for improvements takes place at the EU level. It is expected that these recommendations are then implemented during the remainder of the year. The European Semester thus delivers the economic policy coordination envisaged in Article 121 of the TFEU within the context of the EU's overarching growth and jobs strategy, Europe 2020, and aims to articulate its objectives for each Member State.

The main objectives of the European Semester are 1) to bring about integrated analysis, recommendations and implementation of Member States' and the EU's economic policy (integrated surveillance); and 2) to provide the relevant recommendations at a point in time when they can still be taken into account in the national policy cycle, that is, before national decisions on economic and financial policies are finalised (*ex ante* coordination). Achieving these two objectives would address two central weaknesses of the surveillance regime that existed under the Lisbon strategy, where fiscal surveillance under the SGP on the one hand and economic and employment policy surveillance on the other were undertaken separately.

Figure 1 The European Semester



Source: European Commission, Directorate-General for Economic and Financial Affairs, 'EU Economic Governance', last updated 30 January 2013, accessed at http://ec.europa.eu/economy_finance/economic_governance/index_en.htm on 8 February 2013.

In practice, the European Semester is launched by the Commission's Annual Growth Survey (AGS), which is published in November of the preceding year. The AGS sets out the broad economic policy priorities of the euro area and the EU as a whole. It is discussed in the Council and the basis for policy orientations is endorsed by the spring European Council meeting. Member States are called upon to take into account these priorities and policy orientations in their National Reform Programmes (NRPs), which set out their plans for economic policy reforms during the year ahead, and Stability or Convergence Programmes (SCPs), which provide information on Member States' fiscal policy as required by the SGP. NRPs and SCPs are published at the same time, between the middle and the end of April each year. Based on these reports, the Commission analyses the policy performance of Member States across all relevant policy areas (fiscal, financial and economic), taking into account the economic situation, the implementation of previous recommendations and the plans for the year ahead. In light of this analysis, which is usually presented in May in a Commission staff working document for each Member State, the Commission presents an overall assessment and CSRs in those areas of highest priority for each Member State. The CSRs relate to all relevant policy areas that are covered by the Integrated Guidelines, the preventive arm of the SGP and the Macroeconomic Imbalance Procedure (MIP). The SGP and the MIP are part of the 'Six Pack', which reformed the SGP and introduced the MIP to address some of the weaknesses identified above.

The Six Pack has also introduced an economic dialogue in which the Economic and Monetary Affairs Committee of the European Parliament may invite the presidents of the Council, the Commission and, where appropriate, the Eurogroup to appear before the committee to discuss the general guidance of the AGS, the results of multilateral surveillance, the conclusions of the European Council relating to the European Semester and any information provided to it by the Council. The purpose of this is to enhance the dialogue between the institutions of the Union, in particular the European Parliament, the Council and the Commission, and to ensure greater transparency and accountability.

The legislative package for strengthening economic governance (the Six Pack)[4]

The legislative package for strengthening economic governance (commonly known as the Six Pack, because it consists of six pieces of legislation) entered into force on 13 December 2011 and has since been applied. It has removed the main weaknesses of fiscal surveillance under the SGP that were identified during the crisis (see above). It also introduced a new mechanism for preventing and correcting macroeconomic imbalances, thereby closing an important gap in the surveillance framework. In practice, both the preventive arms of the SGP and the MIP are fully aligned with the European Semester, and their application can result, where relevant, in CSRs for Member States. To the extent that the SGP and the MIP bring about stronger incentives for the implementation of sound policies, they have significantly strengthened the European Semester and the surveillance of economic policy in general. Naturally, it will take some time before the expected results in terms of policy implementation and economic performance can be observed.

Strengthening fiscal surveillance

The Stability and Growth Pact

Several important innovations of the SGP were brought about with the adoption of the Six Pack.[5] First, the existing rule requiring Member States to reach their set medium-term budgetary objective was complemented by a new rule that the rate at which a Member State's expenditures can grow in any given year must be linked to a reference value based on the rate of medium-term potential growth (expenditure benchmark). This new rule was added to the preventive arm of the SGP, whose objective is to avoid Member States breaching the deficit and debt targets in the first place. It should ensure that in the future Member States' fiscal policies will be more prudent and will avoid the mistakes of the past. The possible expansion of expenditure in economic good times will be moderated by the new reference to the medium-term potential growth rate. This should allow buffers to build up that can be drawn on during economic downturns.

Second, the preventive arm of the SGP was also strengthened through a numerical definition of what constitutes a 'significant deviation' from the required adjustment path towards the medium-term budgetary objective. This innovation will allow action to be taken, for example, issuing a warning, at an earlier stage in the process than previously.

Giving the debt criterion of the Maastricht Treaty (60% of GDP) practical meaning in the application of the corrective arm of the SGP is the third main innovation in the SGP brought about by the Six Pack. This has been achieved by making it possible to open an Excessive Deficit Procedure based on the level of debt. Member States with a level of public debt above the 60% threshold are now required to achieve an average reduction in the excess level of debt of one-twentieth per year in order to fulfil the requirements of the rule. This means that a Member State with a public debt level of 80% of GDP (implying an excess of 20 percentage points of GDP above the threshold) will have to achieve an average annual debt reduction of 1 percentage point of GDP.

A significant innovation to the SGP is the introduction of a new voting procedure—the 'reverse qualified majority vote' (RQMV)—for the Council when adopting specific decisions upon recommendation from the Commission in both the preventive and corrective arms of the SGP. Whereas in the past a Commission recommendation for a Council decision required a qualified majority in its favour in order to be adopted, it now can only be stopped if there is a qualified majority in the Council against it. The RQMV will therefore make it much more difficult than previously to stop relevant decisions by organising a blocking minority.

In view of the larger potential negative spillover effects in a monetary union, a financial sanction can be imposed on euro area Member States if recommendations given to them are not followed up with corrective action. This sanction comes in the form of an interest-bearing deposit equivalent to 0.2% of GDP. The relevant Council decision under the preventive arm of the SGP is to be taken by RQMV in which only euro area Member States can take part. Under the corrective arm of the SGP, the interest-bearing deposit

can be converted into a non-interest bearing deposit through a decision by RQMV in the case of a Member State's 'serious non-compliance'. This can be converted (also under RQMV) into a fine of 0.2% of GDP, where non-compliance persists.

Directive on national fiscal frameworks[6]

In addition to the changes to the SGP, the Six Pack also introduced minimum standards for national fiscal frameworks at all administrative levels. Requirements include the adoption of a multiannual planning framework and the application of numerical fiscal rules to promote compliance with the rules of the SGP.

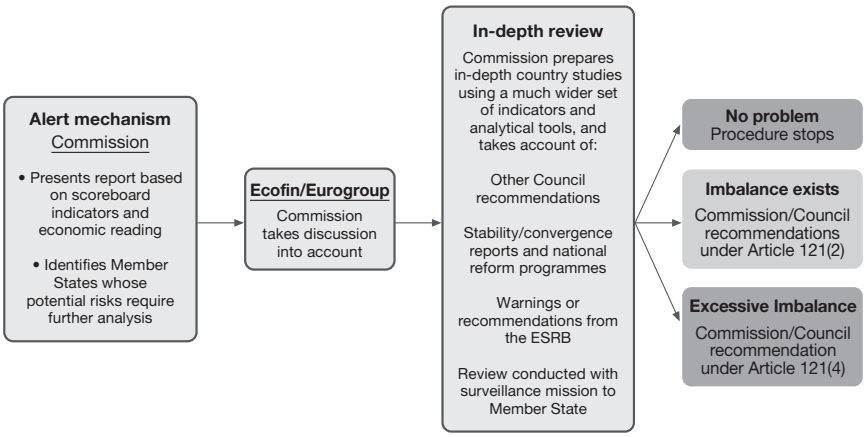
Introducing the Macroeconomic Imbalance Procedure (MIP)

The new MIP is structured analogous to the SGP, that is, it is split into a preventive arm that is fully aligned with the European Semester and a corrective arm (the Excessive Imbalance Procedure) that operates separately and can, in principle, be invoked at any time, if needed.

The preventive arm is launched at the same time as the European Semester through the publication of the Alert Mechanism Report (AMR).[7] The Alert Mechanism consists of a scoreboard of indicators considered relevant for the early detection of macroeconomic imbalances and an economic reading of these indicators. The scoreboard published with the first AMR comprised 10 indicators able to signal internal imbalances such as house price developments, levels of public and private debt, and the evolution of private credit.[8] It also highlighted external imbalances such as the current account balance, changes in export market shares, the net international investment position, and the evolution of a country's competitiveness as measured by the real effective exchange rate and developments in unit labour costs. For each indicator a certain threshold value is set which, if reached, suggests that there could be an imbalance. For some of the indicators (e.g. the current account balance and the real effective exchange rate) a lower and an upper threshold have been set,

implying that both a current account surplus and a deficit, or a rise or fall in the real effective exchange rate, could be indicative of a problem.

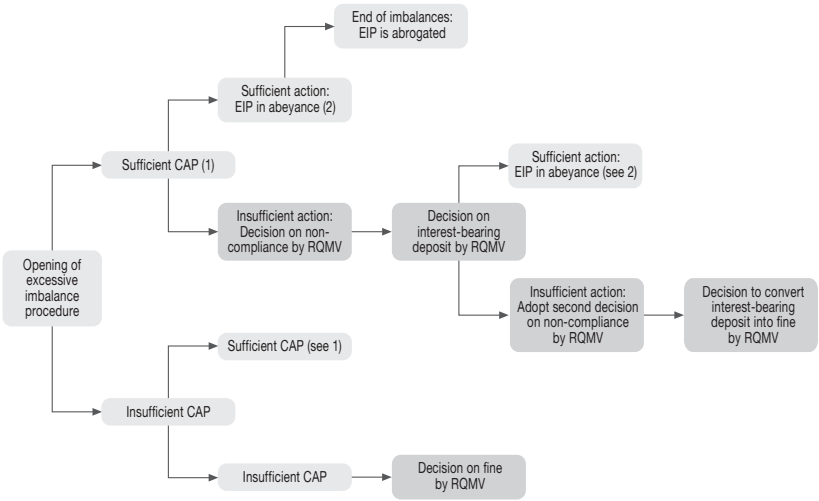
Figure 2 Overview of the two-step approach of the MIP



Source: European Commission, Directorate-General for Economic and Financial Affairs, *The MIP Framework*, accessed at http://ec.europa.eu/economy_finance/economic_governance/macroeconomic_imbalance_procedure/mip_framework/index_en.htm on 18 February 2013.

Neither the scoreboard nor the AMR have the objective of arriving at a conclusion as to whether an imbalance is present in any given Member State. Nor do they offer policy guidance. The Alert Mechanism is merely used to identify those Member States whose economies appear to warrant a more in-depth examination. Where such closer examination is indicated the Commission will prepare an in-depth report, which will be published at some stage during the European Semester and, depending on its findings, may either give rise to CSRs under the preventive arm of the MIP and as part of the European Semester in the case of an imbalance that is not severe, or, where a severe imbalance is found, to the opening of the MIP's corrective arm, the Excessive Imbalance Procedure (EIP). Of course, theoretically, it may also conclude that there is no imbalance.

Figure 3 The corrective arm of the MIP



Notes: CAP: corrective action plan; EIP: Excessive Imbalance Procedure; RQMV: reverse qualified majority voting.
Source: European Commission, Directorate-General for Economic and Financial Affairs, *The MIP Framework,* accessed at http://ec.europa.eu/economy_finance/economic_governance/macroeconomic_imbalance_procedure/mip_framework/index_en.htm on 18 February 2013.

Where the EIP is opened, the Council will issue a recommendation to the Member State concerned and set a deadline for presenting a corrective action plan (CAP). In the CAP, the Member State is required to present concrete measures to address the imbalance that has been identified. If the CAP is inadequate in the view of the Council, the Member State must amend the plan. In the case of repeated failures to provide an adequate CAP or the failure to fully implement it, there is an option to impose sanctions equivalent to 0.1% of GDP on the Member State concerned.

Further strengthening of economic governance in the euro area: the 'Two Pack'

On 23 November 2011, the Commission proposed two additional regulations for the euro area that are commonly referred to as the 'Two Pack'.[9] The first is on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of the excessive deficits of Member States in the euro area (hereinafter the 'Common Provisions Regulation'). The second is on the strengthening of the economic and budgetary surveillance of Member States that are experiencing or threatened by serious difficulties with respect to their financial stability in the euro area (hereinafter the 'Strengthening Surveillance Regulation'). At the end of 2012 these proposals were still under discussion between the European Parliament and the Council, the EU's co-legislators. The rationale for these additional legislative proposals lay in the fact that the lingering euro area sovereign debt crisis appeared to require additional steps, both in terms of ensuring fiscal discipline in order to re-establish confidence, and also in view of the stronger spillover effects at work within a currency union.

The proposal for the Common Provisions Regulation envisages a common budgetary timeline and common budgetary rules in the euro area, additional monitoring requirements for all euro area Member States, and closer monitoring for those operating under the Excessive Deficit Procedure (EDP). The proposal *inter alia* provides for common budgetary rules to be monitored at the national level by independent institutions. It also requires euro area Member States to present draft budgetary plans to the Commission and the Eurogroup by mid-October of each year. Where the Commission finds serious non-compliance with the requirements of the SGP in the draft budgetary plan, it can request the submission of a revised plan. It can also address an Opinion to the Member State concerned which would be subject to discussion by the Eurogroup. For euro area Member States operating under the EDP, the proposal envisages a framework of graduated monitoring to ensure a timely and durable correction of excessive deficits.

The proposal for the Strengthening Surveillance Regulation introduces the concept of enhanced surveillance for Member States experiencing or faced with serious financial difficulties. Enhanced surveillance implies more rigorous reporting obligations from the Member State concerned and closer monitoring by the Commission, including quarterly reports to the Eurogroup Working Group. The proposal envisages that the Commission may independently decide to subject a Member State to enhanced surveillance where necessary. Member States receiving precautionary assistance from the EU's financial assistance mechanisms would automatically become subject to enhanced surveillance. The Strengthening Surveillance Regulation also lays down procedures for decisions on macroeconomic adjustment programmes and introduces the concept of post-programme surveillance, which should apply to countries until they have repaid at least 75% of the debt owed to the relevant financial assistance mechanisms. Another important objective of the Regulation is the simplification of procedures for countries operating under a macroeconomic adjustment programme. In order to achieve this, the Regulation proposes to suspend all reporting under the regular surveillance mechanisms (European Semester, SGP and MIP) for as long as a country is implementing a macroeconomic adjustment programme.

In the course of the negotiations on the Two Pack, an effort was made to integrate some of the provisions contained in the intergovernmental Treaty on Stability, Coordination and Governance in the EMU (see next section) into the two Regulations. In this context, the European Parliament has linked agreement to the Two Pack to progress on politically sensitive dossiers, such as concrete proposals for a European debt redemption fund. At the time of writing, agreement on the Two Pack has not yet been reached between the co-legislators. Such an agreement will probably depend on the progress made with the work on completing EMU, which has been carried forward since June 2012 by the presidents of the European Council, the Commission, the Eurogroup and the European Central Bank (in the 'Four Presidents' Report').

The Treaty on Stability Coordination and Governance in the EMU (TSCG)

The TSCG is the latest addition to the EU's evolving economic governance tableau, which has already been significantly overhauled with the introduction of the European Semester and the entry into force of the Six Pack.[10] When the heads of state and government of the euro area and several non–euro area Member States decided on 9 December 2011 to strengthen economic governance further, they did not originally have in mind an intergovernmental treaty. As far as possible, they were aiming for a limited change of the TFEU. As unanimity would have been required for a treaty change and this could not be attained, all 17 Member States whose currency is the euro and all other non–euro area Member States, with the exception of the United Kingdom and the Czech Republic, eventually signed up on 2 March 2012 for the new intergovernmental treaty. This treaty was ratified by the required number of signatories and entered into force on 1 January 2013. The aim remains to incorporate the provisions of the TSCG into the legal framework of the EU within five years. In part, this might be achieved by incorporating some of its provisions into the Two Pack legislation that is under discussion between the co-legislators at the time of writing. The provisions of the TSCG are binding only for EU Member States whose currency is the euro.

The TSCG consists of three main parts, the Fiscal Compact, a section on economic policy coordination and convergence, and one on the governance of the euro area. Of them, the Fiscal Compact is unquestionably the most important. One of its main features is the incorporation of the key principles and rules of the EU's fiscal governance (i.e. the SGP) into national legal systems. Thus, at its heart, it contains a provision requiring the contracting parties to enshrine in their national legal system, preferably constitutionally, a fiscal rule which ensures balanced budgets. The implementation of this provision will be monitored by the European Court of Justice. The TSCG also sets a ceiling of 0.5% of GDP for structural deficits. Along with this it provides for national automatic correction mechanisms that will be triggered, leading to the implementation of corrective measures, if there is a significant deviation

from the budgetary objective or from the adjustment path towards it. The Fiscal Compact also includes closer monitoring of countries operating under the Excessive Deficit Procedure (EDP), which will have to present an Economic Partnership Programme detailing the measures, in particular the structural reforms, necessary to achieve a timely and lasting return to their medium-term budgetary objective.

In the section on economic policy coordination, contracting parties made commitments to deepening economic policy coordination, including through increased recourse to enhanced cooperation on matters essential for the smooth functioning of the euro area, as well as to systematic *ex ante* coordination of major economic policy reforms among euro area Member States.

Deepening economic and monetary union

The crisis as the driver for economic governance reform

The financial and economic crises of 2008 and 2009, and the lessons learned from them have been the main impulse driving the reform of EU and euro area economic governance. The entry into force of the Six Pack in December 2011 brought about a major overhaul in economic policy coordination. This change was so significant that it would have been inconceivable only a few years earlier. It was possible because the need for Member States to regard their economic policy as a matter of common concern was suddenly plainly evident, not only to economists and policymakers, but to every citizen, in the light of the crisis experience. Taking liberties with economic and financial policy had proven extremely costly, particularly in the euro area. At the same time, there was not necessarily a close link between responsibility for policy mistakes and bearing their costs.

In view of this free-rider problem, some of the major objectives of economic governance reform have been to strengthen discipline, to

sharpen incentives, to introduce credible sanctions early on, and to reduce the degree of political discretion when the Council decides on these matters. For individual Member States, free-riding behaviour has become considerably more costly than was the case before economic governance reform began. With the TSCG, signatory Member States have additionally committed themselves to enshrining the key rules and principles of euro area fiscal surveillance in their national legal systems. Continued close adherence to these commitments should go a long way towards raising credibility and mutual trust, much of which was lost during the crisis.

Apart from the need to address economic policy misbehaviour on the part of Member States, analysis of the financial and economic crisis has also yielded the insight that it was not only wilful breaches of the rules or carelessness that were to blame for the problems of the EU and euro area. The insufficient institutional set-up for EMU had contributed to producing incentives for economic agents that, in the aggregate, led to negative outcomes, such as the severe macroeconomic imbalances that built up in a number of countries. The most striking examples of this were the real estate bubbles and credit booms in Ireland and Spain which started and gained momentum because of very low real interest rates. These were the result of the fact that the business cycles of various euro area economies were not sufficiently aligned and that the single monetary policy for the entire euro area provide one single policy interest rate targeting the euro area average. The respective gap in the EU's economic surveillance set-up was closed with the introduction of the MIP. Other important reforms, such as the creation of a European Systemic Risk Board to identify macro-prudential risks emanating from the financial sector, are important complementary additions for preventing future crises.

The fundamental purpose of economic policy coordination is to ensure the implementation of sound economic and financial policies that bring about stability and lead to strong economic growth and job creation. However, it will be some time before the results of economic governance reform can be seen. The significant improvements made to economic

policy coordination were therefore not sufficient to quell the crisis of confidence that came about in the course of 2011 and continued to fester as self-reinforcing negative feedback loops developed between weaknesses in the banking sector due to concerns about the sustainability of Member States' public finances (as Member States were rightly seen as lenders of last resort to the banking system) and a poor growth outlook. In 2012, the crisis of confidence led to doubts about the very existence of the EMU and the future of the single currency. This happened even with the creation of successively larger and more flexible financial firewalls (the European Financial Stabilisation Mechanism, the European Financial Stability Facility and the European Stability Mechanism), which have the capacity to provide financial assistance to euro area Member States in line with the strict conditionality associated with the implementation of a macroeconomic adjustment programme.

Deeper integration as a response to the crisis of confidence

The crisis of confidence in the EMU and the euro has led to steps being taken towards completing the institutional set-up underpinning the single currency through more fundamental reforms that go beyond policy coordination and envisage integration, that is, involving some sharing/pooling of national sovereignty. In order to achieve this, since June 2012 the European Council has been exploring options for the creation of more integrated financial, budgetary and economic policy frameworks, and for setting down arrangements that can ensure their democratic legitimacy and accountability.

In view of the nature of the crisis of confidence, the creation of a more integrated financial framework and concrete steps towards a banking union are the most urgent elements of the project to create an institutional framework for EMU that permits its strong performance and, where necessary, swift and efficient crisis management. The short-term objective is to break the negative feedback loop between banks' problems and Member States' debt sustainability. Euro area heads of state and government made this clear in their statement on 29 June 2012, in which they called for the

possibility of the European Stability Mechanism to be able to directly recapitalise troubled banks in euro area Member States, that is, without lending the funds to the Member State concerned, and thus without raising the Member State's public debt. This innovation was made conditional on the creation of a single supervisory mechanism (SSM) for EU banks, so as to ensure that the relevant decisions are taken by an independent supranational body not beholden to national interests. The creation of such a single supervisory mechanism is therefore the most urgent element in the discussions. It is also the most advanced as, on 12 September 2012, the Commission made a legislative proposal regarding the SSM that gives the European Central Bank (ECB) a key role. Once the SSM is operational, which is expected to happen in the course of 2013, the Commission will present further proposals to create a fully fledged banking union. These will include progress on a European mechanism for banking resolution, as well as proposals for deposit guarantee insurance.

The decisions of 29 June 2012 and the concrete work on an SSM, as well as the other elements of a complete institutional set-up for EMU, are expected to have an important positive impact on confidence. The announcement by the president of the ECB to stand ready to purchase in the secondary market the bonds of those euro area Member States which have committed to strict reform conditionality through a formal agreement (the Memorandum of Understanding) with the European Stability Mechanism, has had an immediate calming impact on the markets. The objective of these Outright Monetary Transactions (OMT) is to counter the irrational fears of a break-up of the euro area, to safeguard the proper transmission of the ECB's policy stance in the real economy throughout the euro area and to ensure the singleness of monetary policy.[11] The transactions will be undertaken strictly within the ECB's mandate to maintain price stability over the medium term. A necessary condition for OMTs is strict and effective conditionality, attached to an appropriate European Financial Stability Facility/European Stability Mechanism programme.

Compared to the debate on the proposals for an SSM, which are already in the legislative process, the discussions on integrated budgetary and economic policy frameworks and on ensuring greater democratic legitimacy

and accountability are at a much earlier stage. As its input into the Four Presidents' Report, the European Commission presented a Communication entitled *A Blueprint for a Deep and Genuine Economic and Monetary Union: Launching a European Debate*. The Communication presents the rationale, aspirations and achievements of the EMU. It also contains a comprehensive analysis of the causes of the crisis in the euro area. In line with the mandate from the European Council meeting of June 2012 it then sets out actions to be taken over the short, medium and long term to bring about integrated financial, budgetary and economic policy frameworks (see Figure 4).[12]

Figure 4 A blueprint for a deep and genuine EMU: launching a European debate

			A blueprint for a deep and genuine EMU Launching a European debate	Secondary law	Treaty change
ALL ALONG THE PROCESS	SHORT TERM	Within the next 18 months	1. Full implementation of **European Semester** and **Six Pack** and quick agreement on and implementation of **Two Pack**	✓	
			2. **Banking Union:** Financial regulation and supervision: quick agreement on proposals for a **Single Rulebook** and **Single Supervisory Mechanism**	✓	
			3. **Banking Union: Single Resolution Mechanism**	✓	
			4. Quick decision on the next **Multiannual Financial framework**	✓	
			5. **Ex ante coordination of major reforms** and the creation of a **Convergence and Competitiveness Instrument (CCI)**	✓	
			6. Promoting **investment** in the **Euro Area** in line with the Stability and Growth Pact	✓	
			7. **External representation of the Euro Area**	✓	
	MEDIUM TERM	18 months for 5 years	1. **Further reinforcement of budgetary and economic integration**	✓	✓
			2. **Proper fiscal capacity for the Euro Area building on the CCI**	✓	✓
			3. **Redemption fund**	✓	✓
			4. **Eurobills**	✓	✓
	LONG TERM	Beyond 5 years	1. **Full Banking Union**	✓	✓
			2. **Full fiscal and economic union**		✓
			Political union: Commensurate progress on democratic legitimacy and accountable	✓	✓

Source: European Commission, *A Blueprint for a Deep and Genuine Economic and Monetary Union: Launching a European Debate*, Press Release (28 November 2012), accessed at http://europa.eu/rapid/press-release_IP-12-1272_en.htm on 8 February 2013.

One objective of the blueprint Communication is to start a debate on what is required to safeguard the achievements of EMU and to fulfil any unachieved aspirations. In the short term, the completion of the new economic governance framework (the European Semester, Six Pack, Two Pack and SSM) and its full implementation is the obvious starting point. Beyond that, the Commission envisages legislative action in the area of banking union (the single resolution mechanism), economic policy coordination and support for structural reforms (the Convergence and Competitiveness Instrument). In the medium term, the blueprint Communication suggests deeper coordination in the area of tax policy issues and labour markets, and the creation of a fiscal capacity for the euro area to support important structural reforms in a large economy in distress. This capacity would be monitored and managed by an EMU Treasury. Coupled with the power of intervention in the design of national fiscal policies, the blueprint considers the possibility of creating a redemption fund to reduce public debt that rises significantly above the 60% of GDP threshold. The common issuance of euro-bills is also discussed. Both the creation of a redemption fund and the issuance of euro-bills would require treaty changes.

In the long run, this step-by-step and policy-by-policy evolution could lead to a full banking, fiscal and economic union. Such a union would include an autonomous fiscal capacity for the euro area to support Member States in the absorption of asymmetric shocks, while avoiding longer-term transfer flows.

All these steps would have to be accompanied by appropriate democratic legitimacy and accountable decision-making so as to ensure accountability at the levels where decisions are taken. Thus, the European Parliament would primarily have to ensure accountability for EU-level decisions. Democratic legitimacy must also always remain commensurate with the degree of transfer of sovereignty from Member States to the European level.[13]

The Four Presidents' Report presented in December 2012 is closely aligned with the Commission's blueprint Communication, particularly regarding the actions envisaged for the short term.[14] It sees breaking the link between banks and Member States as the most pressing objective.

Therefore, the priority from now until the end of 2013 is to set up the operational framework for direct bank recapitalisation through the European Stability Mechanism (ESM), to ensure approval of the agreed preconditions (an effective SSM) and to ensure the agreement of other relevant legislative proposals (the Capital Requirements Regulation and Directive, proposals on the harmonisation of national resolution, and the deposit guarantee frameworks). Subsequently (2013–14), the integrated financial framework should be completed through the setting up of a common resolution authority and an appropriate backstop to ensure that bank resolution decisions are taken swiftly, impartially and in the best interests of all. The Commission also supports the setting up of a mechanism for the stronger coordination, convergence and enforcement of structural policies based on arrangements of a contractual nature between Member States and EU institutions. On actions that may be taken over the medium and long term, the Four Presidents' Report refers to the Commission's blueprint Communication as a 'basis for debate'.

The European Council meeting of December 2012 partially took up the ideas launched in the blueprint Communication and in the Four Presidents' Report, with a focus on the immediate need for progress regarding the SSM and additional steps towards an integrated financial framework/banking union. The European Council conclusions did not make reference to any medium- or longer-term actions discussed in the Commission's blueprint or the Four Presidents' Report, but defined its agenda in the following way:

> The European Council agreed on a roadmap for the completion of the Economic and Monetary Union, based on deeper integration and reinforced solidarity. This process will begin with the completion, strengthening and implementation of the new enhanced economic governance, as well as the adoption of the Single Supervisory Mechanism and of the new rules on recovery and resolution and on deposit guarantees. This will be completed by the establishment of a single resolution mechanism. A number of other important issues will be further examined by the June 2013 European Council, concerning the coordination of national reforms, the social dimension of EMU, the

> feasibility and modalities of mutually agreed contracts for competitiveness and growth, and solidarity mechanisms and measures to promote the deepening of the Single Market and to protect its integrity. Throughout this process, democratic legitimacy and accountability will be ensured.[15]

State of play and outlook

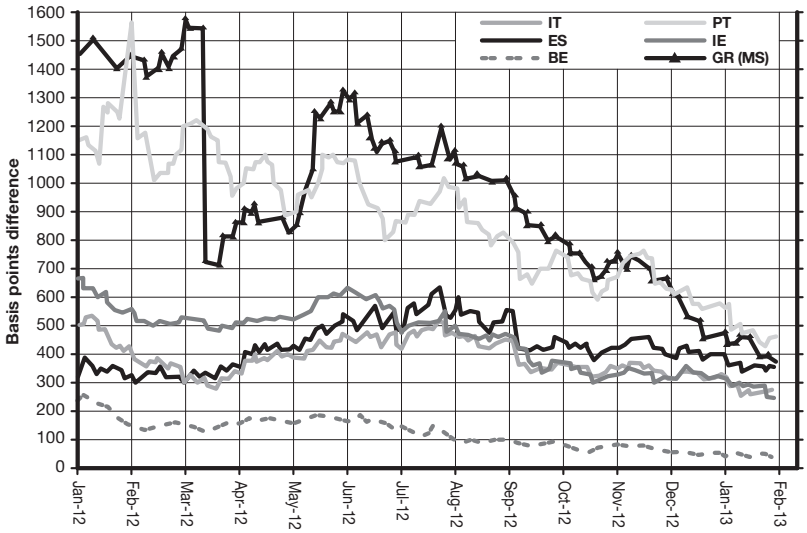
The reform of the economic governance of the EU and the euro area has been an important element in the EU's response to the financial, economic and public debt crises in recent years. Its purpose is to provide confidence that the EU can ensure sound economic and budgetary policies that will generate growth and employment in the future. With the entry into force of the Six Pack, economic policy coordination has been strengthened very significantly. The Fiscal Compact contained in the TSCG has added to these efforts to strengthen confidence in the quality of future economic and budgetary policy through the additional commitments taken on by Member States. The Two Pack has proposed additional steps for euro area Member States and offers the opportunity to incorporate some elements of the TSCG into secondary EU legislation at an early stage.

In 2012 decisive progress was made in addressing the crisis of confidence that had temporarily raised the spectre of a break-up of the euro area. The explicit recognition of the negative feedback loops between banks and sovereigns by heads of state and government at the June European Council meeting and their determination to break them was crucial. The agreement to establish an SSM and to enable the direct recapitalisation of troubled banks by the ESM once the SSM was in place was a concrete step towards breaking the feedback loops. It was also the first step towards a banking union. The June European Council also recognised that for confidence to return in a lasting fashion the EMU would need a more complete institutional framework based on integrated financial, budgetary and economic policy frameworks. The Commission's blueprint Communication and the Four Presidents' Report responded to this call for ideas on deeper integration later in 2012. However, the introduction by the

ECB of the OMTs, which link secondary market purchases of government debt to the strict conditionality of ESM-supported programmes, was decisive in lowering the risk of a break-up of the euro area (the 're-denomination risk').

In combination, these announcements and actions have brought the euro area back from the brink, as is reflected in the risk premiums for Member States facing difficulties, which have been declining in a sustained fashion for more than six months, since mid-2012 (see Figure 5). This achievement can only be secured in a lasting fashion if progress is made with the proposed legislation on banking union and if other pending proposals, such as the Two Pack, are swiftly adopted.

Figure 5 Risk premia: interest rate differences between the government debt of Italy, Spain, Belgium, Portugal, Ireland and Greece compared to German government debt, 10-year bonds



Source: Graph from the Directorate-General for Economic and Financial Affairs; data from *Bloomberg.com*.

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Notes

[1] This article reflects the views of the author and is not attributable to the European Commission. The article draws mainly on published Commission documents, such as *A Blueprint for a Deep and Genuine Economic and Monetary Union: Launching a European Debate*, COM(2012) 777 final/2 (30 November 2012).

[2] European Council, 'Conclusions', 28–9 June 2012, EUCO 76/12 (29 June 2012), accessed at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131388.pdf on 18 February 2013; European Council, *The Euro Area Summit Statement* (29 June 2012), accessed at http://www.consilium.europa.eu/eudocs/cms_data/docs/pressdata/en/ec/131359.pdf on 18 February 2013.

[3] Ibid., 1–3.

[4] European Commission, *Legislation*, Volume 54, OJ L306 (23 November 2011), accessed at http://eurlex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:306:FULL:EN:PDF on 8 February 2013.

[5] For an overview of the changes to the SGP, see European Commission, Directorate-General for Economic and Financial Affairs, 'Report on Public Finances in EMU, 2012', *European Economy* 4/2012, 70–84, accessed at http://ec.europa.eu/economy_finance/publications/european_economy/2012/pdf/ee-2012-4.pdf on 8 February 2013.

[6] Ibid., 85.

[7] European Commission, *Alert Mechanism Report 2013, Prepared in Accordance with Articles 3 and 4 of the Regulation on the Prevention and Correction of Macroeconomic Imbalances*, COM(2012) 751 final (28 November 2012).

[8] The scoreboard has in the meantime been completed by adding a financial sector indi-

cator. European Commission, *Completing the Scoreboard for the MIP: Financial Sector Indicator*, Commission Staff Working Document, SWD(2012) 389 final (14 November 2012), accessed at http://ec.europa.eu/economy_finance/economic_governance/documents/alert_mechanism_report_2013_financial_sector_en.pdf on 8 February 2013.

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[10] For the text of the TSCG, see European Council, *Treaty on Stability, Coordination and Governance in the Economic and Monetary Union*, accessed at http://european-council.europa.eu/media/639235/st00tscg26_en12.pdf on 8 February 2013.

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[12] European Commission, *A Blueprint for a Deep and Genuine Economic and Monetary Union*, 11–34.

[13] For suggestions to ensure democratic accountability and legitimacy, see European Commission, *A Blueprint for a Deep and Genuine Economic and Monetary Union*, 35–40.

[14] Herman Van Rompuy et al., *Towards a Genuine Economic and Monetary Union* (5 December 2012), accessed at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/134069.pdf on 8 February 2013.

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EU Budget Policy

Introduction

The new, wide-ranging responsibilities taken on by the EU in the wake of political decisions made by the Member States bring with them added challenges for the European Community budget. The appropriate definition of responsibilities and the equitable distribution of burdens are thus of primary importance for the continued successful development of the EU. Globalisation has brought topics such as energy, climate change, demography and migration, as well as the resolution of the economic crisis, to the forefront of European debate. In a rapidly changing world, the EU is confronted with questions regarding how these challenges are to be met—and overcome—in the next decade and, furthermore, how the EU budget is to respond to new circumstances. A budget that responds to the priorities of the past but barely meets those of the present cannot serve as a foundation for the future. The budget must function as a dependable and efficient instrument in the implementation of common priorities in order for the EU to remain internationally competitive into the future.

The revenue side of the European budget

Budgetary rights are amongst the oldest parliamentary rights and are seen as an essential prerogative of parliament. In the EU, these rights are shared with the Council by the European Parliament. According to the Treaty of Lisbon, the revenue side of the Community budget remains in the hands of EU heads of state and government due to the 'own resources decisions'. On the expenditure side, however, the European Parliament (EP) is an almost equal partner with the Council in almost all areas.

Apart from various 'specific resources'—such as the dues and contributions of EU personnel, fines collected in the Microsoft case and

income from interest and guarantees—the European Community currently has the four following sources of revenue:

- The customs duties that are collected on imports at the external borders in keeping with the common customs tariff.

- The agricultural duties which were introduced in 1962 in the context of the Common Agricultural Policy and which apply to trade in agricultural products with non–Member States. These vary according to the extent of the price differences on the European and world markets. Apart from agricultural duties, there are also duties on the production and storage of sugar.

- The own resources[1] based on value-added taxes are revenues from the value-added taxes (VAT) of the Member States. As neither the VAT rates nor the lists of goods and services subject to VAT have been harmonised at the EU level, for each Member State a given rate is applied to a base which has been determined in a uniform manner.

- The most important revenues for the EU budget derive from the contributions made by the Member States on the basis of gross national income (GNI). They are determined through the application of a fixed rate, which is arrived at annually according to a budget procedure, to a base which represents the sum of the gross national product at market prices. This own resource is calculated through reference to the difference between expenditures and the yields derived from other own resources. This is the central own resource as it determines the ceiling on the VAT base, the distribution of the costs for the UK rebate and the ceiling on total resources in accordance with the financial perspective.

The traditional own resources based on revenues from customs duties and agricultural duties represent the Union's only genuine own resources, although the Member States tend to consider them national contributions. The smaller the share of these traditional own resources becomes, the more

the EU will become dependent upon what is considered classic intergovernmental transfers. This almost automatically leads to a situation wherein the Member States attempt to optimise national benefit from the EU budget. The more the general feeling arises that revenues have been transferred from the Member States to Brussels and that they do not derive from EU-specific sources, the more the Member States will focus upon what they consider a return service. It is for this reason that the concept of 'budgetary balance' and the roles of net contributors and net beneficiaries have become so important.

Although there is an established system for calculating the contributions of the Member States, at issue is essentially an accounting process concerning the purely financial costs and advantages of the individual Member States vis-à-vis the Union. The discussion—particularly popular in Germany—regarding net contributors may thus be met with the observation that, along with the budgetary benefits of the EU, there are also many benefits that are not immediately quantifiable (for example, the external and internal stabilisation of the Community, German exports within the EU, etc.).

The reform of own resources has for many years been a regular item on the summit agendas of the EU heads of state and government: at the Brussels European Council of 1988; the Edinburgh European Council of 1992; the Berlin European Council of 1999 and the Brussels European Council of 2005.

In contrast to the 1988–99 financial period, when the Member States had provided the EU with significantly more own resources, in particular to ensure financing of the politically desired expansion of funding for the Structural Fund set out in the Delors II package (Edinburgh 1992), the Berlin Summit of April 1999 marked a pronounced change in approach.

Initially, the ceiling of 1.27% for commitments was left unchanged for the financial period 2000–06. Further to this, an effective reduction was undertaken through the introduction of a ceiling for payments at 1.15% of average EU Gross National Product (GNP). This tendency was further

strengthened in Brussels in 2006 as the ceiling for payments was lowered first to 1.24% and then, as of 2010, to 1.23% of EU GNP.

Budget procedures

The approach to the financing of the EU was not changed with the Treaty of Lisbon. The right of initiative is held by the Commission, whereas the Member States remain responsible for fundamental decision-making with regard to the system of own resources. Here, a unanimous decision by the Council is required, which only then comes into effect after having been approved by the Member States according to their constitutional regulations. The rights of the EP are limited to the submission of an opinion within the consultative process. The principle set forth in the current treaties regarding appropriate levels of funding remains unchanged. Article 311 of the Treaty on the Functioning of the European Union (TFEU) states: 'The Union shall provide itself with the means necessary to attain its objectives and carry through its policies.'

This tendency is strengthened, moreover, when taken in conjunction with an essential principle of budgetary discipline: no legislation that has significant implications for budgetary planning is to be passed without assurances being provided that the expenditures associated with the legislation may be financed with Union own resources and in compliance with the Multiannual Financial Framework (MFF).

Moreover, in the Treaty of Lisbon various aspects were clarified and, simultaneously, a first step was taken towards the 'communitisation' of the system. With the Treaty, a new element has been added to the decision on own resources; new categories of own resources may now be introduced and existing categories removed. Essentially, this alteration does little more than provide confirmation of a pre-existing situation. This applies equally to the amounts of these resources, which naturally includes the possibility of changing or withdrawing them or creating new resources.

In order to develop an equitable and, from the perspective of citizens, transparent system of own resources for the medium term, the

implementation of measures for own resources will be stipulated by a regulation of the EP that is to be approved with a qualified majority and the consent of the EP (Art. 311 TFEU). Notwithstanding the restriction that the implementation measures be enacted within the limitations set by the own resources decision, this provision opens the way for an increased role for the EP in matters concerning own resources.

Independently of the Treaty of Lisbon, the EP has occupied itself increasingly with the fundamental reform of own resources in two stages. On 29 March 2007, the plenum of the EP adopted a resolution of the Committee on Budgets (the rapporteur was Alain Lamassoure, European People's Party (EPP)/France).[2] The report confirmed the perception that cumbersome Community procedures made it impossible to adopt necessary resolutions in a timely manner. For this reason, a two-stage approach to the improvement of the current system of national contributions was to be introduced.

The first stage was to find a common basis for all of the Member States. It was possible to arrange this as follows: the share of GNI could serve as the foundation for the contributions of the Member States to the Union's own resources. This stage would be accompanied by the elimination of the VAT own resources in their present form and, ultimately, by the gradual elimination of the UK rebate and all other rebates, for example the 'targeted rebates' and other special benefits.

The second stage was the creation of 'genuine own resources' for the Union. There are, however, various principles which must be taken into consideration when establishing the cornerstones of such a system of own resources. These include full respect for the sovereignty of Member States with regard to taxation; taxation neutrality; preservation of the scope of the EU budget; the progressive introduction of the new system; and, finally, the establishment of a clear political linkage between a reform of revenues and a reform of expenditures.

Further, an important component of the second stage will be the introduction of a new system of own resources on the basis of a share of taxes already collected in the Member States. The revenues from this tax

could, in whole or in part, flow into the EU budget, which would create a direct link between the Union and European taxpayers. This would also contribute to the harmonisation of tax legislation and would constitute a return to a principle set forth in the Treaty of Rome whereby European expenditures were to be financed by European own resources.

The current discussion of relevant taxes that could serve in whole or in part as own resources for the EU has suggested the following taxes: value-added tax, excise duties on fuel for transportation and other energy taxes, excise duties on tobacco and alcohol, taxes on business profit, tax on securities trading, tax on transportation and telecommunications services, income tax, a withholding tax on interest payments, European Central Bank (ECB) profits, environmental taxes, taxes on currency exchanges, taxes on savings, and taxes on financial transactions. In its impact assessment of 28 September 2011, the Commission specifically recommended a new VAT own resource and a tax on financial transactions. All of these 'new' taxes would be bound by the stipulation that they not contribute to an increase in the total revenue. Thus, they would be required to replace other sources of revenue. Attention would also be paid to the terminology used in public in reference to these taxes.

Since his hearings before the EP Committee on Budgets as the 2009 Commissioner candidate, the subsequent Budgets Commissioner Janusz Lewandowski has expressed himself clearly with regard to any new tax. He has publicly claimed that such a tax would not be added to the current EU tax regime, but that the present system, which is complicated and complex even for experts, would be replaced by a new source of financing.

In its proposal of late March 2012, the Commission expressed particular support for an EU-wide financial transaction tax (FTT) of 0.01% as a new source of EU own resources. Altogether, two-thirds of the tax revenues collected within the Member States would enter the European budget, with one-third flowing into national budgets. The GNI-based contributions by the Member States would be reduced relative to their share of FTT revenues. According to Commission calculations, the contributions of the Member

States in 2020 could thus be reduced by approximately €54 billion. The Commission proposal for a new system of own resources intended to provide the EU budget with greater transparency was met with approval in the Committee on Budgets and by the two co-rapporteurs responsible, Jean-Luc Dehaene (EPP/Belgium) and Anne Jensen (Alliance of Liberals and Democrats for Europe (ALDE)/Denmark). Furthermore, with its resolution of 23 May 2012 on the 'Podimata Report', the EP expressed majority approval for a European financial transaction tax as a response to the financial crisis.[3] The Members of the EP approved the introduction of the tax even in the eventuality that individual Member States refuse to participate. The Members of the EP expressed approval for an FTT with a broad tax base across the entire EU.

Excursus: rebates

The UK Rebate was introduced by the Fontainbleau European Council in 1984. Its conclusions state that any Member State sustaining a budgetary burden that is excessive in relation to its relative prosperity may receive the benefits of corrective measures. The problem was originally rooted in the particular situation of the United Kingdom. A country with a small agricultural sector and hence the beneficiary of limited agricultural expenditures from the Union, the UK was confronted with providing a disproportionately large contribution for the financing of the Community budget.

Since then, the rebate has been financed by all of the other Member States according to their respective share of VAT returns. Since 1999, however, Germany, the Netherlands, Austria and Sweden have only paid a quarter of their respective shares. They literally receive a 'rebate from the rebate'. Over the course of subsequent years, it has become increasingly evident that the existence of the UK rebate has led to a significant reduction in the desired balance between the ability of individual Member States to make their contributions and their own resources payments. Moreover, the complexity of the correcting mechanism has contributed significantly to a reduction in the transparency of the own resources system. All in all, there are approximately 30 special rebates for individual projects, regions, Member States and means of payment.

A clear, equitable system is no longer discernible in relation to these special allowances. They emerged from the political deals and package solutions arranged during the negotiations of the heads of states and governments and their finance ministers. Were the rebates to be eliminated, the long history of budgetary privileges would come to an end. Preferable would be a new, simpler and more equitable system that could serve as a possible step in the direction of the introduction of a system of genuine own resources for the Union. All of the Member States that presently contribute to the UK rebate would profit from such an arrangement.

The expenditure side

A closer look at developments on the expenditure side in recent years indicates that the 2000–11 time period saw an increase of 42% in the EU budget and of 62% on average for national budgets. This relatively moderate increase is all the more remarkable given that the Union accumulated a considerable number of areas of responsibility during this period, while the GNI share of the EU budget declined significantly (according to the Commission proposal for the 2014–20 MFF, the decrease during the 1993–2020 time period amounts to 20%).

The annual budgets and the MFF are the most important instruments for the effective implementation and planning of the EU budget. The EU's annual budget is fixed jointly by the Council and the EP according to a detailed procedure. The annual budgets are to remain beneath the ceiling of the Interinstitutional Agreement (IIA), which is agreed upon by the Council, Commission and the EP. The MFF has proven to be quite successful in past decades. Dependability and planning security in particular have increased. The purpose of the MFF is also to improve the annual process of fixing the budget and interinstitutional cooperation in the budgetary sphere, and to ensure the economic management of the budget. Furthermore, the MFF promotes the practical implementation of comprehensive budgetary discipline. Budgetary discipline is binding for all expenditures and all

relevant institutions within the 2007–13 MFF. In the last 25 years, there have been a total of four financial frameworks. Since the Treaty of Lisbon, the MFF, which is to have a term of at least five years, has been set down in the form of a regulation requiring the unanimity of the Council and the assent of the EP.

The current financial framework for the EU of 27 Member States

In 2006, after difficult negotiations within the Council and between different EU institutions, it was finally possible to arrive at an IIA concerning budgetary discipline and the sustainable economic management of the budget for 2007–13. In particular, the EP successfully advocated for an increase in resources for research, life-long learning, Trans-European Networks (TEN), the Common Foreign and Security Policy (CFSP), neighbourhood policy, and the areas of competition and innovation. Furthermore, the current agreement provides for the utilisation of resources from the European Investment Bank (EIB), in connection with EU budgetary guarantees, as catalysts for public and private research investment in the areas of TEN and small and medium-sized enterprises (SMEs).

With the passage of the new IIA, it was also possible to fundamentally reform the EU budget. This provides for more manoeuvrability during the annual setting of the budget, quicker response times to emergency situations, the simplification of the budget and the certification of current programming, as well as improved control mechanisms for the current budget.

Despite these successes, individual problem-areas related to the budget have been left unchanged. Here, a review clause concerning the assessment of decisions until 2013 and the timely preparation of the next financial framework ought to be undertaken.

Together with the payments for the 2007–13 Structural Funds, the portion devoted to agricultural expenditures amounts to €308 billion, which leaves

very little manoeuvrability with regard to the financing of new policy areas or priorities. In the context of a further fixing of total expenditures to approximately 1% of GNI, the question arises of whether, given the resources available, it will actually be possible to meet the targets of the Lisbon Strategy and its successor strategy, Europe 2020, with regard to growth, employment and competitiveness.

Given this financial framework, it has to be asked whether the EU will be in a position to provide the resources necessary for the implementation of its policies and the achievement of its objectives.

The new budgetary procedure

With the Treaty of Lisbon, the annual budgetary procedure was significantly reorganised. The most important change concerns the lifting of the differentiation between obligatory and non-obligatory expenditures. The logical consequence of this change is that the EP and the Council have equal weight in passing the budget plan in its entirety. The rule whereby the EP, the Council and the Commission are required to ensure that the Union possesses the financial resources necessary to fulfil its legal responsibilities to third parties has been left unchanged.

The second change concerns the function of the second reading. This has to do with a procedure by which, due to the particular nature of the legislation, political responsibility is created for the achievement of goals. In the case of a budget 'co-decision', unity is to be sought so that the capacity to act constructively and the continuity of the EU budget are maintained. The Treaty of Lisbon retains a provision concerning the 'interim twelfths': should a situation arise wherein the budget plan has not been finalised by the beginning of the budget year—1 January—monthly expenditures may be undertaken which amount to a twelfth of the previous year's budget. This option became a real possibility during the first budget procedure after ratification of the Treaty of Lisbon, when negotiations on

the 2011 budget were at risk of failure due to the resistance of Great Britain, Sweden and the Netherlands. Ultimately, however, the 'twelfths budget' was avoided with the presentation of a new proposal by the Commission.

Four revisions

The current financial framework has been modified repeatedly. The EU has responded to crises and challenges with four regroupings. These revisions may also be seen as an expression of general dissatisfaction with the present financial framework and the potential it represents. Individual Member States have nonetheless resisted adjusting the MFF. The revisions effected the provisioning of supplementary resources for the Galileo Satellite System in 2007, the financing of a food facility for developing nations in 2008, the allocation of resources for the European Economic Recovery Plan in 2009 and the increasing of the budget for the construction of the International Research Reactor, ITER, in 2011.

External pressure to reform, such as from the EU's stimulus package, has affected the shaping of the EU budget in terms of future-oriented expenditures. The economic crisis revealed that a refocusing of the budget is possible. This has entailed significant institutional negotiation, however, even when only a limited budget was affected (€6.2 billion). This situation has not changed, even with the coming into effect of the Treaty of Lisbon.

Advance preparation of the Parliament's priorities

With the summer 2011 report of the SURE Special Committee,[4] the EP had already established its negotiating position with regard to the MFF as of 2014. Given the number of new responsibilities for the European budget, as well as political commitments (for example the Europe 2020 strategy), there

was agreement regarding an increase in the Community budget of 5% relative to 2013, while retaining the deflator of 2%. Had this proposal not met with support, the Council would have been called upon to establish its negative priorities for the subsequent necessary cuts or to provide for greater flexibility within the MFF as a means of responding to the most urgent challenges within a reasonable time frame.

Furthermore, in the SURE report the EP expressed support for comprehensive reform of the revenue side of the European budget and, in keeping with the EU Treaty, called for genuine own resources which would be allocated entirely to the EU budget. The previous system, based primarily on the GNI share of the Member States, as well as rebates and correction mechanisms, was to be dismantled.

The EP's negotiating position has been strengthened by the Treaty of Lisbon, which has formalised the previously informal process for MFF negotiations. In future, the MFF will take the form of an EU regulation and become legally binding after having been adopted according to the relevant ratifying procedure. The fundamental proposals concerning EU budget issues that are gathered in the MFF regulation may only be put into effect with the consensus of the Member States and upon agreement by all EU institutions. The EP is to remain appropriately informed about the unfolding of the negotiations. Ultimately, there must be majority agreement in the EP with regard to the regulation proposal negotiated between the Member States. Should the financial negotiations fail, according to Article 312(4) of the TFEU, the ceilings are to be carried forward into the individual 2013 budgetary headings until the relevant parties have agreed to a new financial framework.

Upon presentation of the Commission proposal for the coming MFF and on the basis of the SURE report, the EP has created its team of negotiators. Along with the chair of the EP Committee on Budgets, Alain Lamassoure (EPP/France), it consists of the two co-rapporteurs on the MFF, Reimer Böge (EPP/Germany) and Ivalo Kalfin (Socialists and Democrats/Bulgaria), as well as the two co-rapporteurs on own resources, Jean-Luc Dehaene (EPP/Belgium) and Anne Jensen (ALDE/Denmark).

Following the co-rapporteurs 12 October Interim report,[5] the EP adopted the resolution *in the interests of achieving a positive outcome of the Multiannual Financial Framework 2014-2020 approval procedure* on 23 October 2012.[6] The procedure will include a comprehensive assessment of the Commission proposal by the EP's Committee on Budgets and other relevant committees.

The Commission proposal for the 2014 MFF

On 29 June 2011, upon presentation of the proposals for the 2014–20 MFF, the Commission expressed support for the reorganisation of the multiannual EU budget into a more transparent and equitable form. Accordingly, the VAT own resources are to be discontinued and new own resources introduced. The commission specifically encouraged the introduction of a financial transaction tax, as well as a new source of VAT revenues. In return, the contributions of the Member States on the basis of their gross national incomes are to be reduced. Moreover, the often criticised and at times non-transparent system of national rebates is to be replaced by a system of payments in fixed sums. The coming financial framework is to extend over seven years and comprise a total volume of approximately €1 trillion (€1,033 billion according to the revised Commission proposal of June 2012). In total, these committed appropriations amount to 1.08% of the GNI of the 27 Member States of the EU.

In the future, European cohesion policy and the Common Agricultural Policy (CAP) will continue to form the largest financial blocks within the EU budget. The Commission has, however, proposed the nominal freezing of funding at 2013 levels and the redistribution of the resulting savings to other areas. In the first pillar (agricultural direct payments) of the CAP, the proposals suggest a reduction in funding. Furthermore, in the future 30% of direct payments in the first pillar of the CAP are to be dependent upon the environmental measures taken by farmers. For the second pillar (rural development), the Commission has proposed an increase. In total, approximately 37% of the Community budget is to flow into the CAP.

In the future, expenditures for EU cohesion policy are to amount to approximately 37% of the Community budget. In addition to the current categories, a new category is to be introduced for transition regions, those regions whose GDP is 75%–90% of the EU average. A common strategic framework, which applies to the Structural Funds along with the European Agricultural Fund for Rural Development (EAFRD) and the Fisheries Fund, is to establish the common provisions for the administration of funds. Furthermore, the 'Connecting Europe Facility' is to promote the development of infrastructure in the areas of transportation, communication and energy.

The areas of research policy (Horizon 2020) and CFSP are also to see their expenditures increased. Administrative costs are to be reduced by 5% relative to the current financial framework.

Furthermore, the proposal for the coming MFF provides for a significant increase in the 2014–20 time period in the resource administered by the Commission outside of the EU budget. In future, the following will be financed outside the MFF: the European Development Fund, the development of the nuclear fusion reactor (ITER), the European Globalisation Adjustment Fund, the European Solidarity Fund, the EU Emergency Reserve, the reserves for crisis in the agricultural sector, and the initiative for Global Monitoring for Environment and Security. The Commission's intentions met with strong resistance from numerous members within the EP Committee on Budgets who called for budgetary unity and transparency.

By the end of 2011, the Commission had followed up with 57 proposals regarding the legal basis for the European expenditure programmes in almost all policy areas. These legislative proposals were accepted by both the Council and the EP in accordance with commonly agreed upon decision-making procedure. The EP thus repeatedly called for the strict separation of the procedures governing decision-making and assent as a precaution against the prior determination of results.

The negotiations for the upcoming financial framework

With the transition from Denmark to Cyprus of the Council Presidency in July 2012, the negotiations for the 2014 EU financial framework entered a crucial phase. The negotiating box introduced by the Danes, which was developed further under the Cypriot Presidency, has proven an effective instrument for promoting discussion in the Council. Here the core issues and options with regard to revenues and expenditures have been linked to the future MFF in order to foster structured discussion within the Council. Under the Cypriot Presidency, the negotiating box is to be developed further, in keeping with the negotiating process.

This is all the more important, as the starting position within the Council is unusually difficult due to the presence of two opposing groups. One group, 'Friends of the Cohesion Policy', is comprised of 13 mainly Eastern European EU Member States that support the Commission proposal and may potentially even advocate for more funding. The other group, 'Friends of Better Spending', includes Germany, France and five other EU Member States that wish to reduce the coming MFF to 1% of GNI (i.e. €100 billion). Thus, two groups have formed whose expectations for the future financial framework are diametrically opposed.

The EP regards the negotiating box favourably, assuming its ability to ease the process of achieving agreement before the end of 2013 and, in keeping with the terms of the Lisbon Treaty, include the EP within the negotiations. At the same time, however, it insists upon the strict separation of the procedures governing the financial framework and the multiannual programmes in order to avoid any possibility of predetermination with regard to the latter in the context of the MFF negotiations.

Even after conclusion of the informal General Council in Nicosia, Cyprus at the end of August 2012, the negotiating positions of individual Member States within the Council remained deeply divergent. For this reason, the original ideal of negotiating the MFF at the Brussels Summit of the heads of

state and government on 18–19 October was reconsidered. Instead, a special summit was agreed upon for the end of November 2012. On 8 February 2013 the heads of state and government reached agreement on the MFF for 2014–20. However, the European Parliament has already expressed the view that it cannot accept the Council's deal as it is but will vote on the proposed MFF later in 2013.

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Notes

[1] The revenues that automatically flow into the EU budget on the basis of treaties and rules of implementation and that do not require further decisions from the individual national authorities.

[2] European Parliament Resolution 2006/2205(INI) of 29 March 2007 on the future of the European Union's own resources, accessed at http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P6-TA-2007-0098&language=EN on 14 February 2013.

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[6] European Parliament Resolution 2011/0177 (APP) of 23 October 2012 in the interests of achieving a positive outcome of the Multiannual Financial Framework 2014-2020 approval procedure, accessed at http://www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&reference=P7-TA-2012-360 on 7 March 2013.

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Taxation Policy in the EU

Introduction

Deeper integration of the single market necessitates a coherent taxation policy. Of central importance is the removal of obstacles both to the cross-border activities of companies and to the mobility of labour. Taxation policy can, after all, contribute to the attainment of broader political goals and to the stimulation of the economy.

Common rules in the area of indirect taxation are necessary to ensure that Member States do not skirt the rules regulating the free exchange of goods nor erect new obstacles after the dismantling of customs barriers. It was for this reason that harmonised rules on indirect taxes were established; in the case of value added tax (VAT) this is also linked to the fact that it is an important source of revenue for the EU.

Contrary to the common misconception that Europe interferes in too many areas, in direct taxation, particularly income tax, but also corporate tax rates, Europe has no authority, nor does it seek any. The work of the Commission in this area sometimes creates conflicts with Member States, which defend their tax sovereignty, at times vehemently, in order to protect their revenues. Yet, notwithstanding the principle of subsidiarity, Europe must take action whenever tax regulations pose obstacles to the functioning of the single market.

Harmonisation of taxes, but to what degree?

According to Article 113 of the Treaty on the Functioning of the European Union (TFEU), the Union is required to harmonise value added taxes and excise duties as well as various indirect taxes to the extent necessary for the establishment and functioning of the single market. Regulations concerning

the harmonisation of taxes—in contrast to most areas within the single market—must be adopted unanimously by the Council. The European Parliament is only consulted on tax legislation; it has no joint decision-making powers. The adoption of the Treaty of Lisbon has changed nothing in practical terms concerning the current division of competence on taxation, although efforts were made in the context of the Convention[1] to introduce a qualified majority for various sub-areas, such as policies against tax fraud and tax evasion. Unanimity also explains why EU progress in the area of direct taxes has been slow.

There is no mandate for the harmonisation of direct taxes. Article 114(2) explicitly states that rules governing new legislation towards the establishment of a single market do not apply to taxation. Thus, authority to legislate in the area of direct taxes is based on Article 115, which allows for approximation of national legislation related to the single market by unanimity.

Also with regard to direct taxes, obstacles which discourage businesses from making cross-border investments are to be eliminated. Furthermore, distortions of competition which arise as a result of differing tax systems are also to be removed. For businesses, the tax burden is often an important, if not decisive, factor for or against making an investment in many locations.

In recent years, the European Court of Justice (ECJ) has issued ground-breaking decisions in the area of direct taxes. These have concerned such matters as cross-border loss compensation, the treatment of dividend payments made in another EU Member State or coming from another EU Member State, and foreign corporate financing. In contrast to the Commission, however, the ECJ renders decisions on a case-by-case basis and must proceed in this manner in removing tax barriers within the single market; it cannot establish positive law. The Commission is responsible for ensuring that discrimination on the basis of taxation is avoided and that all companies are guaranteed a level playing field.

In its Communication of 23 May 2001, *Tax Policy in the European Union—Priorities for the Years Ahead*,[2] the Commission developed a

comprehensive strategy for taxation policy. This Communication proposes the closer coordination of taxation policy with the general goals of the EU. Above all, the taxation system should not impede individuals or businesses from profiting from the single market. Fair competition between tax systems should also continue to be possible. There is no need for a general harmonisation of the taxation systems of the individual Member States. Each state is free to choose an appropriate taxation system, as long as it respects EU regulations. Action at the EU level would be required only if it was impossible to resolve problems based on actions taken by individual states. Many problems in the realm of taxation require nothing more than the better coordination of national policies to ensure the exercise of basic freedoms and to remove tax obstacles to cross-border activity. Of relevance here is the prevention of double taxation and double non-taxation, improved coordination against tax evasion and tax avoidance, and the fight against harmful tax competition. Given that the single market is more strongly affected by various indirect taxes, the Commission holds that a greater degree of harmonisation is necessary in this area.

Regulations in the area of direct taxes

The elimination of discrimination against cross-border companies

At the end of the 1960s and throughout the 1970s, the Commission submitted a series of proposals concerning company taxation. In particular, these proposals pertained to cooperation between businesses operating across Member States and the harmonisation of systems of corporate taxation. For a long time, however, the Council was unable to agree on their implementation. Only the directive concerning mutual assistance by the competent authorities of Member States in the field of direct taxation and the taxation of insurance premiums was passed relatively quickly, in 1977.[3] It enables the exchange of information between tax administrations with regard to the setting of these taxes. This exchange of information does not take place when it conflicts with the legal

regulations or the administrative practices of a Member State (for instance, when banks are required to uphold the confidentiality of customer information against the demands of a tax administration). In 1990, a breakthrough was achieved in the field of direct taxes: three of the measures in the area of direct taxes proposed by the Commission in 1969 were passed. These measures are outlined below.

The merger directive

This directive on a common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares which pertain to businesses operating in several Member States ensures that cross-border mergers or merger-like procedures are not disadvantaged relative to equivalent domestic procedures.[4] To this end, the undisclosed reserves of the acquiring company are taxed only when they have been realised. The scope of the merger directive was extended on 17 February 2005 by Council Directive 2005/19/EC[5] to include additional companies subject to corporate taxation, as well as to European limited companies and European cooperative societies. Other forms of restructuring were also affected.

The parent company–subsidiary directive

This directive concerning the common system of taxation for parent companies and subsidiaries in different Member States is intended to prevent the multiple taxation within the Union of the profits of foreign subsidiaries.[6] The Member State of the parent company either does not tax the profits earned from the foreign subsidiaries or credits the taxes already paid abroad against domestic taxes. Furthermore, the profits sent by the subsidiary to the parent company are no longer subjected to tax deductions at source. Any company located in a Member State which holds a capital share of at least 25% in a company in another Member State (subsidiary) is considered a parent company as outlined in the annex to the Council Directive. The parent company–subsidiary directive was amended by Council Directive 2003/123/EC of 22 December 2003[7] to extend its scope so that the minimum holding

percentage for claims to tax advantages was progressively reduced from 25% to 10% in 2009. The mechanisms for the prevention of double taxation were also improved. Along with other kinds of corporations, European limited companies and European cooperative societies were also included.

Arbitration agreement

The convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises provides for an arbitration procedure to adjudicate differences of opinion between financial authorities in the case of tax corrections for transfer pricing between associated enterprises.[8] It is meant to ensure that double taxation is completely eliminated within three years of the launching of a process of arbitration. The Arbitration Convention came into effect on 1 January 1995 and was initially approved for five years. It was later renewed and extended to include the new Member States.[9]

Combating harmful tax competition (taxation package)

Intensified tax competition within the EU increasingly led Member States to introduce ever-lower tax rates and competitive tax regimes as a means of attracting potential investors. As this detrimental tax competition was eroding the tax base, the Economic and Financial Affairs Council passed a package on 1 December 1997 to combat harmful tax competition, and instituted the following measures on 3 June 2003.[10]

Code of Conduct

This imposes the legally non-binding though politically relatively important responsibility on Member States to refrain from (standstill responsibility) or to take back (rollback responsibility) potentially harmful taxation measures in the area of business tax. Whether a measure is to be included or not is determined according to specific criteria, such as whether an advantage is granted exclusively to non-residents or for the transactions of non-residents, or whether advantages are actually based on economic

activity. The code refers to taxation measures (legal and administrative regulations as well as administrative practices) which have or could have a significant influence on a company's choice of location. In support of the code, the Council has established a board made up of representatives of the Commission and the Member States (Code of Conduct Group) which assesses relevant national measures and, if necessary, deems them harmful. In total, more than 400 regulations and practices have been analysed as a result of the Code of Conduct. More than 100 were judged harmful, causing them to be eliminated or abandoned.

Work towards the Code of Conduct was successful in part because simultaneous efforts were underway at the OECD to combat harmful tax competition. The OECD produced a list of tax oases and established a forum on tax dumping.

The directive on interest and royalty payments

According to the directive on a common system of taxation for interest and royalty payments made between associated companies of different Member States, all taxes at source on interest and royalty payments between associated companies of different Member States are to be abolished.[11] Taxation at source on interest and royalty payments made by companies based in other Member States is potentially disadvantageous for cross-border enterprises due to higher administrative costs or double taxation. This cannot be solved only through recourse to the domestic measures of the Member States or in the context of a double taxation agreement. The directive is applicable to interest and royalty payments between associated companies in different Member States and includes payments between production sites and associated companies.

The taxation of income from interest payments in the Community

Council Directive 2003/48/EC of 3 June 2003 on the taxation of interest earnings is meant to ensure that every citizen of the EU pays tax

on the interest earnings accrued in a different Member State.[12] This does not entail an alignment of tax regulations. Since 1 July 2005, Member States have automatically exchanged information concerning interest payments made to residents in different Member States. Only Luxembourg, Austria and Belgium were temporarily allowed to introduce a withholding tax with a rate that would rise progressively from 15% in 2005 to 20% in 2008 and 35% as of 1 July 2011. They are required to transfer the tax yield to the country of origin of the recipient of the interest earnings. While Luxembourg and Austria continue to follow this arrangement, on 1 January 2010 Belgium adopted the exchange-of-information regime.

The coordination of national systems of taxation in the area of direct taxes within the single market

As indicated above, the Commission holds that a coordinated approach to direct taxes is necessary as a means of eliminating obstacles within the internal market. Thus, it has presented proposals on a coordinated approach to the elimination of taxation obstacles and inefficiencies in direct taxes. In order to proceed incrementally, the Commission has increasingly chosen to use such non-binding instruments as suggestions and Communications, rather than submitting legislative proposals. In particular, the following Communications have been issued.

In its Communication of 22 November 2006,[13] the Commission examined a workable approach to tax incentives for research and development (R&D). The Communication explains the legal obligations which derive from EU decisions and presents various fundamental principles as well as best practices for the implementation and coordination of tax incentives. The Member States are encouraged to improve the implementation and coordination of tax incentives in the area of R&D. The Communication also offers an orientation to the Member States with regards to the various fundamental approaches possible. In its Communication *The Elimination of Tax Obstacles to the Cross-Border Provision of Occupational Pensions* of 19 April 2001,[14] the Commission proposed a comprehensive strategy for

eliminating tax restrictions for both private citizens who wish to join a pension plan outside their country of origin and for pension providers that wish to offer their services across borders. It stipulates that, according to the ECJ, the deductibility of contributions to pension providers in other Member States is not to be denied.

In its Communication concerning the coordination of Member States' direct tax systems in the single market of 19 December 2006,[15] the Commission determined that taxpayers in situations of cross-border activity are often discriminated against, double-taxed or required to expend extra costs to ensure compliance with legal requirements. This Communication is directed at coordinating and improving the performance of unharmonised direct tax systems. Coordination can extend from the specific individual measures of the Member States, such as changing domestic law, via bilateral measures, such as the establishment or alteration of agreements on double taxation, to Community-wide measures. As a first step, the Commission expressed its intention to develop guidelines for the numerous decisions of the ECJ. In terms of further steps, it announced several initiatives for a coordinated approach among the Member States. With these measures, it hopes to eliminate discriminatory handling and double taxation, prevent non-taxation and abuse, and reduce compliance costs.

In its Communication *Tax Treatment of Losses in Cross-Border Situations* of 19 December 2006,[16] the Commission provided an overview of the tax treatment of losses within a company or group of companies in domestic and cross-border situations. Furthermore, on the basis of decisions by the ECJ, this Communication explains the basic principles and problems of cross-border loss relief and how Member States could allow it in instances where losses are sustained either within a company (that is, by a branch or a permanent establishment of the company in another Member State) or within a group of companies (for instance, by a group member in another Member State). Within the EU, an efficient system of cross-border loss relief is to be established as a means of avoiding discrimination against cross-border companies or groups of companies.

To avoid the unfair treatment and double taxation of taxpayers who move to another Member State, in its Communication of 19 December 2006,[17] the Commission called upon Member States to better coordinate their individual systems of rules with regards to exit tax. Many Member States levy taxes on capital gains when taxpayers move their place of residence or assets to another Member State. This increase in value was first taxed domestically when it was made, that is, when the assets were sold. In this Communication, the Commission examines how the applicable exit tax rules of individual Member States, which apply to individuals and companies, could be made compatible with EU law. Guidelines were also formulated as to how the rules of individual Member States could be coordinated with one another to eliminate double taxation, unintended non-taxation and abuse, and to prevent the erosion of the tax base.

In its Communication of 10 December 2007, *The Application of Anti-abuse Measures in the Area of Direct Taxation–Within the EU and in Relation to Third Countries*,[18] the Commission called on Member States to examine their guidelines for combating abuse in the area of direct taxes in the context of EU law and to seek coordinated solutions. In order to prevent the transfer of business-related incomes to other countries and the erosion of tax bases, Member States formulated regulations for combating the abuse of tax rules. As has been established by numerous decisions of the ECJ, these regulations occasionally contravene the basic freedoms of the EC Treaty. According to the Commission, the ECJ had set down clear criteria for individual circumstances whereby the anti-abuse measures must be established according to purely artificial constructs: that is, to cases not involving actual establishments or to situations where no real commercial interests are concerned. Beyond this, however, the extent to which these principles could be applied to the particular circumstances for which they had been established remained to be determined. In this regard, the Commission emphasised that despite the basic freedoms of the treaty, the Member States must retain the ability to prevent the erosion of their tax bases due to unintentional non-taxation or the abuse of tax regulations. The Commission would also like to initiate a general discussion of possible

constructive and coordinated responses to challenges and to examine the applicability of these principles beyond the particular circumstances of individual cases.

The prospects for further harmonisation in the area of direct taxes

The coordination of corporate taxation

The existence of 27 different tax systems, the difficulties of complying with transfer pricing formalities and the absence of cross-border loss compensation, as well as the tax costs arising from cross-border restructuring, all contribute to the creation of enormous additional costs for companies. In this area, the single market is not yet as efficient as it could be. In its attempt to eliminate these obstacles, the Commission is taking a two-pronged approach: targeted measures, such as the establishment of a forum for transfer pricing, and a comprehensive attempt to find appropriate solutions. All companies active in the EU should be able to determine their EU corporate tax base according to a single set of tax rules. In the long term, the Commission sees the introduction of a common consolidated corporate tax base (CCCTB) for multinational companies active across the EU as the only way to reduce the tax obstacles for companies active in more than one Member State.

To this end, on 16 March 2011 the Commission presented a *Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)*.[19] The goal of the CCCTB is to allow companies to submit their corporate tax return in a single location. Points worth mentioning include,

- the CCCTB represents a broad, unified and simplified tax base with as few exceptions as possible;
- companies based in the EU will report their total income on the basis of the CCCTB;
- the system is optional for corporations; and

- the corporate tax base will be divided between the Member States according to a special formula which contains the following three factors: assets, labour and sales.

The corporate tax rate of each Member State determines the portion provided to them. In order to protect national sovereignty, corporate tax rates are not harmonised.

The CCCTB is an important initiative in the context of the Europe 2020 vision of the Barroso II Commission. It is also referred to in a series of policy papers which are intended to remove single market obstacles and to promote growth and employment in the EU (*Single Market Act, Annual Growth Survey* and *the Pact for the Euro).*

The extent to which it will be possible to realise the goals of the CCCTB is questionable, however, given the principle of unanimity, and particularly as the alignment of the corporate tax base, including the regulation of specific administrative procedures, extends deeply into the tax sovereignty of Member States. Tax efficient Member States such as Ireland have sharply criticised this proposal. Should some Member States choose not to participate, as is probable, the Commission is considering a proposal whereby those states that wish to implement it will be able to do so in the context of intensified cooperation.

The taxation of interest payments

On 15 September 2008, the Commission published a report on the directive on the taxation of interest payments as well as a related working paper. The report covered the implementation of the directive, a first assessment and possible improvements. The report concluded that the directive, although effective, had reached the limits of its applicability. Indirectly, if not measurably, it had had the positive effect of enhancing taxpayer compliance. Due to the many gaps in the scope of application, however, the Commission thought it necessary to include a broader range of beneficiaries and transactions and to improve a number of procedural

aspects. On 13 November 2008, the Commission passed a proposal to amend the directive on the taxation of interest payments in order to close loopholes and better prevent tax avoidance.[20] To this end, interest payments earned by intermediary, tax-free structures (certain foundations or trusts) are to be more efficiently taxed. Furthermore, the application of the directive is to extend to income that corresponds to interest from assets in particular financial arrangements as well as particular life insurance products.

As requested by the Council on 9 June 2009, talks with Switzerland, Lichtenstein, San Marino, Monaco and Andorra are being held on the alignment of the current agreement in keeping with the proposed amendments to the directive on interest tax. A review is also to take place of the actual implementation of the OECD standards concerning the exchange of information, standards which these states are politically obliged to follow. Furthermore, discussions are being held with other financial centres (Hong Kong, Singapore and Macao) concerning the possible application of equivalent rules in the area of interest taxation. On the basis of a mandate extended by the Council on 25 September 2008, the Commission is negotiating with Norway concerning a specific agreement on the application of similar measures.

Combating tax fraud

The *Proposal for a Council Directive on Administrative Cooperation in the Area of Taxation*[21] was intended, as of 1 January 2010, to replace the directive on administrative assistance.[22] This proposal was formally passed on 15 February 2011 in the ECOFIN Council. The directive aims to strengthen mutual assistance by Member States in the area of taxation and ensures that the OECD standard for the exchange of information upon request is maintained in the EU. The directive would extend and improve the flow of information in various ways, thus contributing to the more effective combating of tax avoidance and tax fraud in the EU. Unlike the former directive on administrative assistance, which was limited to direct taxes and insurance premiums, the new directive also includes all indirect

taxes. The only exemptions are for those taxes which, like the value added tax or excise taxes, are subject to special EU regulations. The directive contains regulations concerning cooperation, in particular with regards to common rules of procedure, documentation and standard forms as well as channels for the exchange of information. In the future, tax administrators are to have the powers of inspection—even within the jurisdiction of another Member State—necessary to allow them to conduct their investigations. Member States are not to resort to policies of banking confidentiality as a means of refusing cross-border cooperation. Finally, Member States are to be obliged in the future to work as closely with EU partners as with third countries.

The directive, likewise proposed by the Commission on 2 February 2009, concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures was passed by the ECOFIN Council as Council Directive 2010/24/EU on 16 March 2010.[23] Its purpose is to promote more efficient assistance between the tax administrators of the Member States in the setting and recovery of taxes. It replaces the recovery directive in the codified form of Council Directive 2008/55/EC.[24] It came into effect on 1 January 2012. In contrast to the former recovery directive, its scope of application extends to all of the taxes and duties levied by Member States and their territorial authorities as well as compulsory social security contributions.

The exchange of information without prior request concerning the tax refunds of tax authorities and foreign residents is to be set forth in binding form. The tax authorities of Member States are to be allowed to conduct their investigations freely within the jurisdictions of other Member States. Administrative assistance should be requested at an early stage in the procedure as a means of improving the likelihood of success.

The taxation of the financial sector

In response to requests by the European Parliament, among others, for increased taxation of the financial sector in the wake of the financial and

economic crisis, the Commission responded, first with a Communication, and on 28 September 2011 with the presentation of a directive proposal[25] related to this issue. In essence, this concerned the coordinated introduction of a new tax. Along with participation by the banks in meeting the costs of a crisis partially caused by them, such taxation is also to lead to the appropriate participation of the financial services sector, which is exempt from the value added tax, in consolidating the general budget. Finally, it should also have a corrective effect by lowering the elevated acceptance of risk shown by players in the financial sector.

In this regard, two alternatives were initially discussed: a tax on financial transactions (FTT) and a financial activity tax. The Commission finally decided to propose a tax on trade in specific products between financial institutions, that is, securities, bonds, shares and derivatives at a minimum rate of 0.1% (0.01% for derivatives). Transactions in which small and medium-sized enterprises or households are involved are explicitly excluded from the tax. In order to reduce the risk of tax evasion, the Commission has proposed that the tax be levied based on the residence principle, that is to say the tax will be due in the country in which the financial institution is established. The tax would become due as soon as one of the institutions involved is resident in an EU Member State. The Commission has furthermore estimated that the tax could yield €57 billion in additional revenue per year and has proposed that a part of this should go to the EU budget as a new own resource.

However, given the unwillingness of certain Member States to agree to an FTT on the EU level, 10 Member States have in the meantime requested to proceed with the introduction of the FTT based on enhanced cooperation. The Commission has reacted positively to this request and formally asked the Council to authorise the enhanced cooperation in this area on 23 October 2012.[26]

Regulation of indirect taxes

Harmonisation of the value added tax

Since the beginning of the common market, the emphasis of the Community in the area of tax harmonisation has clearly been on indirect taxes. The intention was to eliminate distortions of competition and fiscal frontiers. In addition, the EU derives a significant share of its own resources from the value added tax. The highest degree of harmonisation has been reached in this area: Member States are not allowed to introduce comparable taxes alongside the unified value added tax.

In order to create the single market and to remove fiscal frontiers between the Member States, the Commission suggested a 'definitive' value added tax system. This system would be based on the principle of taxation in the country of origin whereby VAT would be levied at the rate applicable in the country of the producer. However, the Member States insisted on maintaining the principle of taxation in the country of destination where goods or services were delivered between companies (the 'provisional' VAT system). In cases of cross-border purchases by private individuals, however, the country of origin principle applies: that is, goods are taxed in the country of purchase. Exceptions apply after the purchase of a specified amount of specific excise goods, to new automobiles and to certain distance sales. In such cases, taxes are levied in the state of destination. VAT rates are approximated, with the minimum standard rate being 15%. Furthermore, there is a political agreement not to exceed the upper limit of 25%. Apart from this, Member States may apply one or two reduced tax rates of at least 5% to the goods and services listed in Annex III of the VAT directive.[27] There are, however, a number of exceptions.

Harmonisation of excise duties

In order to create the single market by 1 January 1993, it was necessary to harmonise the structures related to the most important

excise duties on tobacco products, mineral oils and alcoholic beverages. At the same time, minimum tax rates were introduced in order to limit competitive distortions and harmful tax competition as well as to reduce incentives for the illegal trade in these goods.[28] For excise duties, the country of destination principle was maintained—that is, as a rule, these commodities circulate under duty suspension. Taxes are levied only in the country of consumption.

The directives on taxation of mineral oils were amended on 1 January 2004.[29] The scope of application was extended to all energy products that serve as motor or heating fuel (including coal and natural gas alongside mineral oils), as well as electricity. A series of industrial sectors (mineralogy, for instance) remain out of the scope of the directive. The minimum rates of taxation for mineral oils, which had not been altered since 1992, were increased. Energy products used in stationary motors or for agricultural purposes can be taxed at a rate lower than fuels used in automobiles. The directive allows for a distinction between the taxation of diesel used as motor fuel for commercial and non-commercial purposes. For the former, a lower rate of taxation can be set, provided it is not less than the minimum rate established in the directive or the applicable national taxation rates of 1 January 2003. Fuels used in commercial air navigation and maritime transport between Member States and with third countries are to be tax free, as are fuels used in the production of electricity, as electrical energy is taxed at the point of consumption. Member States may also apply a number of additional tax exemptions or lower rates of taxation, as long as these do not affect the proper functioning of the internal market. For example, renewable energy sources, including biofuels and fuels used for the transport of goods and passengers by train, metro, tram and trolley bus can be exempted. Lower minimum rates of taxation are applied to heating fuels for commercial use than those for private use. Furthermore, energy intensive businesses and industrial sectors that have committed to alternative measures leading to environmental protection objectives or increased energy efficiency may also, under certain conditions, be taxed at a level lower than the minimum rate.

Prospects for the further harmonisation of indirect taxes

The most important issue to be resolved in the establishment of a definitive value added tax system has long been the question of whether to move to the country of origin principle as previously provided for by the Commission. However, Member States have been unable to agree to the Commission's plans to institute a definitive VAT system in five stages, as suggested in the Communication of 10 July 1996, *A Common System of VAT: A Programme for the Single Market*.[30] In its Communication of 20 October 2003, *Review and Update of VAT Strategy Priorities*,[31] the Commission took stock of the proposals forwarded in the context of the strategic programme for the value added tax and elaborated a new vision for a VAT system which would be relevant to the requirements of a single market with 25 Member States.

Reduced value added tax rates

With the acceptance of Council Directive 2009/47/EC of 5 May 2009 amending Council Directive 2006/112/EC concerning reduced rates of value added tax,[32] all Member States are permitted to continue to apply reduced rates of value added tax on specific locally sourced labour-intensive services, including hotel and restaurant services, for which there is no danger of causing unfair competitive imbalances between service providers in different Member States. Reduced rates of value added tax were previously allowed for locally sourced labour-intensive services on a temporary basis and based on case-by-case requests by Member States. According to the Council directive, all Member States that so wish may now apply a reduced rate of value added tax to the services in question, which include bicycle repairs, household cleaning, domestic care, hairdressing services, renovations and repairs to private dwellings (with the exception of materials, which contribute a considerable portion of the value of the service), and restaurant and catering services. Books printed on all forms of physical material (excluding e-books) may also be subject to a reduced rate.

Calls are repeatedly made to allow reduced rates of value added tax for green products—that is, energy saving materials and energy efficient

products and services. In March 2008, the European Council issued a request to the Commission to investigate this matter. As a result of subsequent discussions, Council Directive 2009/47/EC allows the application of reduced rates to renovations of apartments, with the exception of materials, which contribute a significant portion of the value of this service. This was the result of a compromise given diverging views among Member States regarding the relevance of reduced rates for green policy objectives, which was also reflected in the statement adopted by the Economic and Financial Affairs Council of 10 March 2009 that 'reduced VAT rates as a tool for achieving environmental policy objectives are relevant only to a certain extent'.[33]

In its Communication on the future of VAT[34] the Commission announced that, following an intensive consultation process, it intends to come forward with new proposals for reorganising the system of reduced rates before the end of 2013. This particularly aims to abolish reduced rates which are an obstacle to the functioning of the internal market or for goods and services of which consumption is discouraged by other EU policies. Finally, the revision will also address the challenge of convergence between the online and physical environments.

Combating value added tax fraud

The present VAT system, which includes tax exemptions for deliveries from one company to another within the EU, can be prone to VAT fraud. All of the Member States agree on the goal of combating fraud. Discussions concerning VAT fraud revolve around two types of measures: conventional measures, which would strengthen the current system, and more far-reaching measures, which would alter the system by, for instance, allowing Member States the possibility of introducing a general reversal of tax liability (general reverse-charge system) as well as the taxation of intra-EU transactions. In February 2008, the Commission presented a Communication on the two far-reaching measures regarding changes to the VAT system to fight fraud.[35] In it, the Commission considers whether the intra-EU transactions which are currently tax free

ought to be taxed or whether the option of a general reversal of tax liability (reverse-charge) ought to be introduced. As the ECOFIN Council was unable to come to a clear orientation concerning these matters, conventional measures have been given more attention for the time being.

Conventional measures relate to such issues as the improvement of administrative cooperation or procedural matters. On 16 December 2008, the ECOFIN Council approved a directive and a regulation stipulating that the collection and exchange of information regarding intra-EU transactions is to be accelerated. In cases where fraud is suspected, tax administrators in the destination countries are to be more quickly informed about intra-EU transactions into their jurisdiction. They will thus be able to respond more quickly than before.

In parallel to this, on 1 December 2008, the Commission issued a Communication[36] which contained a temporary action plan with a list of future legislative proposals intended to increase the efficiency of investigations by tax administrations and prevent VAT fraud, as well as to enable the recovery of defrauded taxes. This Communication also contains longer-term reflections concerning the relationship between taxpayers and tax administrations and, in particular, the possibilities made available by advances in information technology.

In response to new forms of fraud—in particular, the rapidly increasing occurrence of carousel fraud with certificates for greenhouse gas emissions—the Commission presented a proposal on 29 September 2009 concerning an optional limited application of the reverse-charge system for providers of specified goods and services. Apart from emissions certificates, the Member States are allowed to apply this system on up to two products from the following list: computer chips, mobile telephones, precious metals and perfumes. Thus, all Member States are provided with the same possibilities for action against this form of carousel fraud. Previously, only Great Britain had been granted this option as a derogation. The possible introduction of the reverse-charge system by the Member

States is to be seen as a pilot project and is thus presently limited to 2014 and contingent on the fulfilment of specified responsibilities concerning evaluation and assessment. An agreement in principle on the proposals was reached in the Council on 2 December 2009 and the new rules entered into force in 2010.[37]

A VAT strategy

With the submission of a Green Paper on 1 December 2010,[38] the Commission introduced a process for the comprehensive restructuring of the current value added tax system. This process is intended to conclude with the adoption of a new strategy for the coming decade. The process proceeds from the consideration that the value added tax is going to become ever more important for state finances and that the current VAT structure contains weaknesses and is, in various respects, out of date.

With regards to cross-border transactions, the determination has been made that it is time to decide upon a definitive system, regardless of whether this system will be established on the basis of the country of origin principle or, as is presently the case, on the basis of taxation in the state of destination. At present, national and intra-EU transactions are treated differently; in the latter, the customer is, as a rule, required to pay the tax. This discriminatory treatment, which also leads to fraud, could either be eliminated through general application of the reverse-charge system or by means of a tax on cross-border deliveries, with the provider paying the tax according to conditions applying in the destination state.

The Green Paper also raises a number of other questions which do not relate specifically to the issue of cross-border transactions. Along with practical aspects of taxation policy, it refers to more general goals, such as the desired neutrality of the VAT system and whether the current degree of harmonisation in Europe is sufficient. In this regard, the Green Paper notes that current variations in the standard rates across the EU, as well as the reduced tax rates of individual Member States, do not appear to be causing difficulties within the single market. Nonetheless, there is a lack of

transparency and, at times, coherence with regard to the reduced rates when, for example, these are applied to such classic cultural products as books but not to competing digital media products (e-books).

The Green Paper initiated an open debate on these questions which the Commission followed up with the publication of a Communication on the future of VAT in December 2011.[39] In this paper the Commission clearly acknowledged that a more ambitious reform of the present fragmented VAT system will be needed to remove barriers to intra-EU trade, but that this reform will have to be based on the country of destination principle given that the principle of taxation in the country of origin will remain politically unachievable. At the same time it is emphasised that a modern VAT system will have to be simpler and more efficient, meaning, for example, that businesses should only have to deal with tax authorities in one Member State.

The further alignment of excise duties

In the area of energy taxation, in 2007 the Commission had already described the principles of a comprehensive restructuring of the current system in its Green Paper on market-based instruments for environmental and related policy purposes.[40] In essence this would lead to a reform of EU minimum rates for energy products which would be split into two components in order to clearly identify and quantify the environmental element of the tax rates currently applied: the current minimum rates based on quantity (in the case of fuels, per 1,000 litres). This should in the future be replaced by minimum rates based on the energy content (in GJ) and on CO_2 content. The tax component based on energy content is to be applied at the same level to competing energy products in order to avoid competitive distortions between different energy sources. The tax component based on CO_2 content ensures that the harmful effects on the environment of various motor and heating fuels are expressed in the tax system. In principle, the latter component is only to be levied if the corresponding energy use is not already captured by the EU emissions trading system. Thus, the instruments of tax and of trade in certificates would be used complementarily.

On 13 April 2011, the Commission presented a proposal for a directive to amend Council Directive 2003/96/EC on restructuring the Community framework for the taxation of energy products and electricity. The proposal provides for minimum tax rates taking into consideration both the CO_2 emissions and the energy content of these products, an approach which conforms to the principles of the Green Paper.

To this end, the minimum tax rate is divided into the following two components:

1. taxation on the basis of the energy product's CO2 emissions at a minimum rate of €20 per ton of CO_2; and

2. taxation on the basis of energy content, that is, according to the actual energy contained in the product as measured in gigajoules (GJ) at a minimum tax rate of €9.60/GJ for motor fuels and €0.15/GJ for heating fuels.

Out of social policy considerations Member States are allowed to exempt energy sources used for domestic heating purposes, regardless of the form of energy used.

Long transition periods extending until 2023 for the complete alignment of taxation based on the energy content of fuels will provide businesses with time to adapt to the new tax structure.

In the area of tobacco taxation, the Commission is pursuing the goal of reducing tobacco consumption and the negative health effects associated with it by increasing EU minimum rates. A Commission proposal from 2008 envisaged a progressive increase of the minimum tax on cigarettes and fine-cut tobacco until 2014.[41] Furthermore, the large difference in tax rates between the two products, which has led to a shift in consumption from cigarettes to fine-cut tobacco, is to be reduced. At present the level of tobacco tax diverges widely across the various Member States—by up to 600% for cigarettes. An increase in the minimum rate, and a reduction in the

difference between tobacco products, is also meant to assist in the struggle against intra-EU tobacco smuggling, which makes it difficult for the Member States to reach their health policy targets by means of an increase in tobacco prices. The Council of the European Union was able to reach a political agreement on the proposed directive. Based on this, a codified version of the EU *acquis* on tobacco taxation was adopted on 21 June 2011.[42] As a result, a number of definitions have been updated and minimum rates on cigarettes and fine-cut tobacco are to be progressively increased until 2014. Several Member States were granted transition periods for the introduction of the new minimum rates; on the other hand, quantitative limits may be applied to imports out of those states in which the new minima do not yet apply.

A final area where unified regulation has not been achieved, despite the efforts of the Commission, is the taxation of passenger cars. At present, upon the permanent transfer of a passenger car into another Member State, a registration tax is usually payable, assuming a national registration tax exists. To eliminate the resulting obstacles to the trade in used vehicles, in 2005 the Commission suggested the progressive elimination of registration taxes.[43] For the transition period, a system of reimbursement was to be introduced which would provide compensation for the registration tax paid in the state of export; this was intended as a means of avoiding double taxation. For environmental reasons, it was also proposed to shift a part of the tax base for circulation taxes to the CO_2 emissions of the relevant vehicle. Council negotiations on this proposal have been suspended since November 2007, as four Member States have questioned the right of the EU to initiate legislation in this area. Nonetheless, in the meantime, a number of Member States have converted their passenger car tax in whole or in part into a CO_2 emissions tax. Regarding registration taxes, the ECJ has in the meantime determined that, when levied on a car previously registered in another Member State, the loss in value for used vehicles has to be considered. Nonetheless, the problem of double taxation in case of transfer of a used vehicle into another Member State has not been resolved because there is no right to compensation for a registration tax previously paid in the country from where it is exported. The Commission is currently considering the prospect of directing relevant recommendations to the Member States.

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Notes

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Dr Rüdiger Dohms

Competition Policy and State Aid Control

Introduction

Competition as an ordering principle for an open and social market economy

From the beginning of European integration, the fundamental decision for a competition-oriented market economy in a single market was laid down in the founding treaties, first at European Community and then at European Union level. According to Article 4(1) of the previous EC Treaty (TEC) and Article 119(1) of the Treaty on the Functioning of the European Union (TFEU),[1] Member States and the Community/Union have had to carry out an economic policy 'conducted in accordance with the principle of an open market economy with free competition.' In line with the fact that this basic principle has always been realised in conjunction with social objectives, the EU Treaty, as reformulated by the Lisbon Treaty (TEU), now contains as one of its objectives an explicit commitment to a social market economy. According to Article 3(3) of the TEU, the EU 'shall work for the sustainable development of Europe based on balanced economic growth and price stability, a highly competitive social market economy, aiming at full employment and social progress, and a high level of protection and improvement of the quality of the environment.'

The decision for an open and social market economy with free competition is based on the experience and conclusion that the free play of supply and demand in goods and services markets is the best guarantee of the most economically sensible use of production factors, the fullest satisfaction of consumer wishes at acceptable conditions, and of economic growth, employment and technical progress. One of the most important conditions for the successful functioning of a market economy is that effective competition prevails among economic players, both on the supply side and on the demand side. This does not prevent responsible states and international organisations from regulating markets in order to

ensure they function sustainably (for example, during the financial market crisis which began in September 2008) and in order to achieve aims of general interest, such as public security and order, social security, and consumer and environment protection, which are not automatically guaranteed by market forces and the competition principle. Good policy therefore strives for an optimal balance between market dynamics and the necessity for regulation on the basis of the principles of proportionality and better regulation.

Undertakings can restrict or remove competition completely by their behaviour in the market (for instance through agreements between competitors or abuses of a dominant market position to the detriment of other competitors or consumers) or through changes to the market structure (for instance mergers and acquisitions of undertakings). Competition can also be distorted by state interventions such as subsidies in favour of certain domestic undertakings and economic branches, or by the special treatment of state-owned undertakings and of legally privileged undertakings. This results in the necessity for binding rules to protect competition and for an effective mandatory control of their application by national or European authorities and courts.

The realisation of the single market (Art. 3(3) TEU), in other words the elimination of all obstacles to the free movement of goods, people, services and capital between Member States (Art. 26(2) TFEU), includes, according to Protocol No. 27 (which is attached to the TEU and the TFEU and is an integral part of both treaties), a system for 'ensuring that competition is not distorted'. The essential elements of a free market economy are thus guaranteed by the four basic economic freedoms and competition. In addition to this, the treaty rules on tax (Arts. 110–13 TFEU) and the approximation of laws (Arts. 114–18 TFEU) deal with the problem of competition distortions, which arise from the different national legal and administrative regulations. According to Article 173 of the TFEU, the Union and the Member States ensure that the necessary conditions for the competitiveness of industry in the Union are guaranteed by means of an industrial policy, and, to this end, they can take specific supportive

measures, although these must correspond to a 'system of open and competitive markets'. Finally, a successful competition policy has several points of contact with consumer protection policy (Art. 169 TFEU), due to its orientation towards consumer interests.

Important trends in EU competition policy since the year 2000

In recent years, all aspects of EU competition have been increasingly aligned with the Lisbon Strategy (adopted in March 2000 by the European Council and further developed in 2005), as well as with the EU 2020 strategy that succeeded it in 2010. Effective competition policy and control of state aid can contribute considerably to this overarching economic reform and growth agenda by promoting price stability and innovation, by preventing state aid races between Member States that would be damaging for public budgets, by securing the benefits of integration in the single market, by protecting consumers from cartels and the abuse of dominant market positions, and by opening up previously monopolised markets.

In order to better fulfil these objectives, even after the expansion of the EU in 2004 and in a continually changing economic context, European competition policy has been comprehensively modernised since the end of the 1990s. It now concentrates on examining the economic effects of a certain conduct in the market, that is, whether a conduct leads to a distortion of competition, thus adversely affecting the interests of consumers and/or the competitiveness of industry, and how effective remedies can be found. At the same time, legal regulations and procedures have been simplified, room for manoeuvre for undertakings without market power has been expanded, the requirements triggering competition law control have been modified, and the relationship of legal enforcement competences between the EU and Member State levels has been partly re-ordered in line with the subsidiarity principle. This allows the Commission, as the European Union's competition authority, to concentrate on the cases in which the functioning of the single market is affected.

In order to promote understanding and acceptance of competition policy, the Commission is constantly working on new publications, produces numerous communications addressed to other EU institutions on specific issues and offers a comprehensive Internet presence.[2] Moreover, since 1999 it has strengthened its contact and cooperation with other EU bodies and institutions; these links have meanwhile been formalised in various inter-institutional agreements and protocols.

The effective legal instruments, which are indispensable for the success of any competition policy, have also been maintained since the entry into force of the Lisbon Treaty. Thus, the core provisions of EU competition law (Arts. 81, 82, 86, 87 and 88 of the TEC) have been left untouched apart from some minimal changes (Arts. 101, 102, 106, 107 and 108 of the TFEU).

The subject matters of EU competition policy in detail

EU competition law applies only to cases in which undertakings are involved. The European Court of Justice (ECJ) follows a very broad definition of an undertaking, including every entity which exercises an activity of an economic nature, in other words, activities of an industrial, craft or commercial nature which are designed to offer goods or services in a market and therefore serve more than self-sufficiency purposes. Neither the legal form of the entity (public or private), nor the type of its financing, nor whether this entity is profit-oriented or even makes any profit is important.[3] In addition, the precondition for the application of EU competition rules is that the matter is not a purely domestic one, meaning that an effect on trade between at least two Member States cannot be ruled out, and that in the area of merger control certain turnover thresholds are reached. As new markets open up and the European single market expands, the number of non-economic or purely domestic cases is decreasing. This proves the comprehensive significance of competition law, which can in principle play a role in all areas of life.

Control of the market behaviour of undertakings (antitrust law)

This part of EU competition law aims to protect the consumer and the single market by preventing undertakings from coordinating their behaviour instead of competing with each other, and by preventing market-dominant undertakings from abusing their position to the detriment of competitors, business partners or consumers.

Article 101 of the TFEU: the prohibition of competition-restricting agreements and concerted practices between undertakings

Article 101(1) of the TFEU prohibits all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market. Article 101(1) of the TFEU therefore prohibits actual restrictions of competition as well as behaviour which creates the concrete risk of such restrictions. It thereby comprehensively protects competition in all its current and potential forms, and at all stages of the economic process. In addition to some vertical competition restraints, Article 101(1) of the TFEU in particular prohibits agreements and concerted practices at a horizontal level, that is, between undertakings at the same stage of the economic process. Included in this category are the so-called hard-core cartels, in which the participating undertakings, for example, coordinate their purchase or selling prices or other trading conditions, share markets or sources of supply geographically or with respect to customers or bids, agree on production or sales quotas or on import and export restrictions, and/or decide on measures against other competitors to damage competition. Such restraints of competition mean that the participating undertakings need make no or significantly less effort to win and retain customers through competitive prices, improved quality or innovation, thus compromising the interests of the consumer and the competitiveness of the economy.

According to Article 101(3) of the TFEU there is an exception to the prohibition in Article 101(1) of the same treaty with respect to individual

agreements or categories of agreements[4] if it can be said that the positive economic effects of the competition restraint outweigh its negative effects. To this end, four conditions must be cumulatively met:

1. The agreement must help to improve the production or distribution of goods or to promote technical or economic progress.

2. Consumers must be allowed a fair share of the resulting benefit.

3. In line with the principle of proportionality, restrictions which are not indispensable to the attainment of these objectives must not be imposed on the undertakings concerned.

4. Such undertakings must not be afforded the possibility of eliminating competition in respect of a substantial part of the market concerned.

In addition, the Commission has been empowered by the Council to enact various block exemption regulations, in which certain categories of competition-restricting agreements are automatically exempted from the prohibition in Article 101(1) of the TFEU under the specific conditions in Article 101(3), which must then be respected by the Commission, national authorities and courts.

Article 102 of the TFEU: the prohibition to abuse a dominant market position

Article 102 of the TFEU prohibits the abuse of a dominant market position in the internal market, or in a substantial part of it, by one or more undertakings insofar as this may affect trade between Member States. A single undertaking is dominant if by means of its economic power it is in a position to effectively prevent competition in the relevant market because it is able to act largely independently of its competitors, its purchasers and ultimately the consumers without suffering any damage itself. Assessment of this should be based on an overall view of the relevant market and the relative position in this market of the undertaking in question. A market share

of 50% or more almost automatically indicates a dominant position. Moreover, several undertakings can hold a collective dominant market position if externally they are as strong as a single dominant undertaking and if internally there is no real competition between them.

Article 102 of the TFEU does not prohibit the holding of a dominant market position, only its abuse. This means all practices of the dominant undertaking which hinder the maintenance or development of the remaining competition in the relevant market through means that deviate from normal competition on merit. Abuse is therefore an objective term; motivations and intentions are irrelevant and fault is not required. In the case of exploitative abuses, the economic dependence of business partners and consumers is exploited, for example, through enforcing disproportionately high prices or other particularly disadvantageous business conditions. Exclusionary abuses are aimed at hindering the expansion of the remaining competitors in the market or hindering the market entry of potential competitors through, for example, various forms of refusal to do business, binding purchasers, fidelity rebate systems, package deals or predatory pricing.

The enforcement of Articles 101 and 102 of the TFEU

Council Regulation no. 1/2003/EC[5] (applicable since 1 May 2004) has improved the implementation of EU antitrust law (Arts. 101–2 TFEU) through more effective instruments and the complete involvement of national competition authorities and courts alongside the European Commission. The Commission has since concentrated on those cases affecting several Member States, whilst the national competition authorities deal with cases whose major effect is within their country. Domestic courts decide whether violations of EU antitrust law have led to the invalidity of agreements and establish claims for injunction or compensation. In this system, the necessary coherence and a reasonable level of legal security are guaranteed for the different users of EU antitrust law through the cooperation of the Commission and the national competition authorities in the European Competition Network, and also through the (mostly voluntary) cooperation between national courts and the Commission. Furthermore, Regulation no.

1/2003/EC defines the procedural rules for the Commission's antitrust work: its powers of investigation (requests for information, sector inquiries and on-site inspections, including the right to question natural persons, to seal business premises and to investigate the private homes of staff members), the hearings of the parties concerned and of third parties, the protection of business and professional secrets, and sanctions (fines and penalties) for lack of cooperation from undertakings in an investigation and for the violation of Articles 101(1) or 102 of the TFEU. In the latter case, undertakings committing a violation may be fined as much as 10% of their worldwide annual turnover.

Merger control (market structure control)

Principles and basic assessment criteria

Effective competition is restricted when a single undertaking or group of undertakings has too much market power, in particular when it holds a single or collective dominant market position. It is therefore necessary not only to subject the behaviour of market-dominant undertakings to the control of abuse under Article 102 of the TFEU, but also to control competition-restricting changes to the market structure, in particular the establishment and strengthening of a dominant market position. In EU law, however, such control only takes place where the change in the market structure occurs as a consequence of a concentration, in other words, a lasting change in the control of the undertakings involved (either through merging two previously independent undertakings, through the takeover of one undertaking by another, or through the establishment of an independent joint venture).[6] However, many concentrations also have positive effects, in particular through synergies which are reflected in research and development, as well as in the increased efficiency and competitiveness of the merged undertakings, and which lead to new or improved products at more reasonable prices for the end user. This is why EU merger control does not prohibit concentrations per se, but only those through which effective

competition in the internal market or in a substantial part of it would be significantly impeded, in particular as a result of the creation or strengthening of a dominant market position.

The legal framework

The EU Merger Regulation, which first entered into force in 1990,[7] protects effective competition and, by means of its clear assessment criteria, speedily provides undertakings with legal and planning security for their projects.

The EU Merger Regulation establishes a clear either/or system with regard to the distribution of competences between the European Commission and national competition authorities: if the concentration has a Union dimension, it falls under the exclusive responsibility of the Commission, and only the Commission must be notified of the project and not the competition authority of any Member State. Undertakings therefore have the advantage of a one-stop shop in the EU. A concentration has a Union dimension if the participating undertakings (irrespective of the location of the undertakings' headquarters) exceed certain annual turnover thresholds worldwide and in the EU: specifically, a combined aggregate worldwide total annual turnover of all participating undertakings of more than €5 billion and an EU-wide annual turnover of each of at least two of the participating undertakings of more than €250 million.[8] A merger without a Union dimension falls under the competence of one or more Member States, and their national merger control rules are applied.

According to the principle of preventive merger control, the Commission must be notified of all planned concentrations which fall under the EU Merger Regulation and they may not be implemented until the Commission has decided that they are compatible with the internal market. Should the Commission at the end of the first phase of the merger control procedure (which normally lasts 25 working days) be of the opinion that the project cannot be cleared (even after any commitments have been offered), and that

the project continues to raise serious doubts as to its compatibility with the internal market, then a more in-depth examination is carried out in a second phase (which normally lasts 90 working days). At the end of this second phase, the Commission makes a final decision that

1. the project is compatible with the internal market and is therefore cleared,

2. the project will be compatible with the internal market after the undertakings involved have committed themselves to modifications (the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with their commitments), or

3. the project is incompatible with the internal market and thus prohibited and may, therefore, not be implemented.

The liberalisation of economic sectors and issues concerning services of general economic interest (including public services)

Numerous interventions by Member States into economic life run counter to the goal of an open and competitive internal market. This is where the rules addressed to the Member States on the basic freedoms of the internal market (free movement of goods, services, capital and workers, and freedom of establishment) and on the control of state aid apply. As a complement to these rules, the antitrust and merger control rules described above ensure, among other things, that the freedoms of the internal market are not undone by the behaviour of undertakings. Finally, this is perfected by the basic principle laid down in Article 3(3) and Article 4(3) of the TEU, in conjunction with Protocol No. 27, which in turn in conjunction with Articles 101/102 of the TFEU, states that Member States, due to their obligation of loyalty to the EU, may not take or maintain any measures which would obstruct the practical effectiveness of the competition rules applicable to undertakings or would threaten the goal of undistorted competition in the internal market. Member States

may not therefore force or induce undertakings into anti-competitive practices or strengthen the effects of such practices. As *lex specialis* here, Article 106(1) of the TFEU obliges Member States, with respect to public (that is, state-controlled) undertakings and undertakings to which they have granted special or exclusive rights (for instance, monopoly or oligopoly positions), not to enact or maintain in force any measures contrary to the rules in the TFEU and the TEU, in particular the prohibition of discrimination and the competition rules.

In the case of public or private undertakings to which a Member State has assigned the task of providing clearly defined services of general economic interest, Article 106(2) of the TFEU allows for the possibility of exemption if and insofar as the unrestricted application of the EU internal market and competition rules would in law or in fact hinder the performance of the particular tasks which the Member State has entrusted to these undertakings. This possibility for exemption applies exclusively to services of general interest (including public services) of an economic nature, as services of a non-economic nature (on which, see below) are per se not covered by EU competition and internal market law. Article 106(2) of the TFEU is to be interpreted narrowly and according to strict proportionality criteria. In other words, the application of the EU internal market and competition rules can be restricted, if at all, only insofar as it is absolutely necessary for the proper functioning of the public service or service of general economic interest.

Article 106(3) of the TFEU enables the Commission, through the enactment of directives or decisions, to specify in general rules or in individual cases the obligations of Member States as laid down in Article 106(1), as well as their ability to shape policy under Article 106(2) of the TFEU. This is a very effective instrument for liberalising of economic sectors (including sectors which supply services of general economic interest) in which Member States have restricted or prevented competition by granting exclusive or special rights (that is, by the creation of monopolies and oligopolies). So far, the Commission has used this instrument in around 16 individual decisions (mainly in the areas of air and sea transport, as well as

the postal and telecommunications markets) and for several directives for the gradual (and finally complete) opening up of the telecommunications sector.

Control of state aid according to Articles 107–9 of the TFEU

Introduction

Increasing competition in a system of European and worldwide free trade and the liberalisation of many economic sectors place undertakings and sectors under growing pressure to adapt; they also raise expectations that the state should intervene to help. State aid granted for these or other reasons which favours certain undertakings or production sectors and distorts or potentially distorts competition and restricts trade between Member States, runs counter to the objectives of an open and competitive internal market and also impairs the competitiveness of undertakings and economic sectors as a whole. Article 107(1) of the TFEU therefore declares that such state aid is, in principle, incompatible with the internal market and thus prohibited; Article 107(2–3) of the TFEU, however, allows certain exceptions under the control of the Commission.

The concept of state aid that is incompatible with the internal market

According to Article 107(1) of the TFEU, a prohibited state measure amounts to any state aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.

Preferential treatment occurs when the recipient, irrespective of the objective of the state action, obtains an economic advantage without

delivering a consideration which is sufficient and customary in the market. This can be either a financial payment or an exoneration for the recipient. Aid can therefore *inter alia* take the form of any of the following: direct subsidies, reduced-interest loans, exemption from tax and social contributions, deferral of loan repayments, guarantees with particularly favourable conditions, the takeover of the costs of a social plan, acquisition of industrial land or property at reduced costs, free access to infrastructures, state allowances for public undertakings or state equity participation in private undertakings.

Preferential treatment is only considered to have been granted by the state or from state resources if public budgets have had resources or income deducted. These budgets may be budgets of the Member State itself or of its territorial authorities (such as regional states and municipalities), or budgets of state-established public or private institutions.

The requirement of selectivity (that is, the explicit or at least factual favouring of certain undertakings or sectors of production) distinguishes state aid from general state measures in economic, infrastructure, tax, employment or social policies, which benefit the entire economy of a Member State indiscriminately.

Selective preferential treatment distorts or threatens to distort competition and affects trade between Member States when it intervenes in a real or potential competitive relationship between undertakings in a relevant market and when there is the trade of goods or services between Member States in this market. A specific intensity of restriction of competition or trade (for example, appreciability) is not necessary. A restriction of trade can be excluded only in cases of a purely local dimension. According to the *de minimis* regulation[9] subsidies not exceeding a maximum of €200,000 per undertaking over the current and previous two tax years are not state aid in the sense of Article 107(1) of the TFEU, and thus need not be reported to the Commission.

Exceptions to the prohibition of state aid: compatibility of aid with the internal market

Article 107(2–3) of the TFEU lays down several exceptions to the basic prohibition of state aid. The Commission controls the application of these exemptions and must be notified in advance of all new state aid. The aid categories named in Article 107(2) of the TFEU are de jure exempted from the basic prohibition of state aid and must therefore be approved by the Commission if it is proven that all the conditions for this legal exception are fulfilled. Included are, in Article 107(2)(a), aid of a social nature granted to individual consumers; in Article 107(2)(b), aid to make good the damage caused by natural catastrophes or exceptional events; and in Article 107(2)(c), aid as a consequence of the German separation (since 1996 this has only been applicable in a few exceptional cases).

In addition, Article 107(3) of the TFEU names five categories in which state aid is subject to a discretionary assessment and may be considered compatible with the internal market:

- 3(a): aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment. This is one of the justifications for regional aid, which is discussed below.

- 3(b): aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State. This basis is used, for example, in individual cases for approving aid for large research projects such as EUREKA, as well as in the intensified financial and economic crisis since 2008.

- 3(c): aid to facilitate the development of certain economic activities or of certain economic areas. This is the most commonly used legal basis, particularly relied upon for approving horizontal aid (for environmental purposes; research, development and innovation; small

and medium-sized enterprises; employment and training; rescue and restructuring, and so on), as well as regional aid.

- 3(d): aid to promote culture and heritage conservation. This is the basis for approving aid, for example, in the field of film promotion, broadcasting and theatre.

- 3(e): such other categories of aid as may be specified by qualified majority decision of the Council. This exception is linked to respecting the basic prohibition of state aid and is very rarely used in practice. Until now it has only been applied in ship building and coal mining.

Decisions on the first four categories are at the discretion of the Commission, which is only subject to very limited control in this matter from the ECJ and therefore exercises extensive economic policy steering power. The Commission carries out an evaluation of the potential distortion of competition and trade on the one hand, and the positive effects of the aid on the other. This evaluation is governed by proportionality criteria used to judge to what extent the aid serves the fulfilment of clearly defined objectives of general interest, which are compatible with Article 107(3) of the TFEU (for example growth, employment, cohesion and protection of the environment).

The enabling regulation, no. 994/1998/EC,[10] empowers the Commission to enact regulations which declare certain categories of aid compatible with the internal market, in the sense of Article 107(3) of the TFEU (provided certain conditions are met), and which thus exempt these categories of aid from the obligatory notification under Article 108(3) of the TFEU. Since August 2008, there has been a General Block Exemption Regulation (GBER),[11] which covers (subject to conditions) certain aid schemes, some individual aid awards based on schemes and some ad hoc aid. The GBER is directly applicable Union law and allows Member States to grant unproblematic aid more quickly and with less bureaucracy. Meanwhile, the Commission can concentrate on the potentially more competition-distorting aid outside of the GBER. In the case of aid for which notification is

necessary, the Commission publishes the criteria by which it will assess the compatibility of aid with the internal market in guidelines, Community frameworks and communications. Such instruments increase legal security, transparency and predictability in the way in which the Commission exercises its discretionary powers and can, according to the case law of the ECJ, create a self-binding effect for the Commission.

Article 107(3)(a) of the TFEU forms the basis for the approval of regional aid in 'areas where the standard of living is abnormally low or where there is serious underemployment.' This criterion is not measured according to the national average, but rather the EU average (NUTS-II regions with a per capita buying power standard of less than 75% of the average in the EU25, that is, not including Romania and Bulgaria).[12] This is necessary in order to prevent a race amongst the Member States for subsidies to be given to particular regions and to stave off a threat to the convergence goals of the EU structural and cohesion funds.

Article 107(3)(c) of the TFEU covers aid for other kinds of (national) problem regions, namely 'aid to facilitate the development . . . of certain economic areas'. This means Member States can support regions which are disadvantaged in comparison to the national average. The Commission also decides which regions qualify for this exemption, based on proposals by the Member States. The Member States can use national criteria to justify their proposals.

The criteria for judging regional aid are laid down in the guidelines on national regional aid 2007–13,[13] on the basis of which the Commission has approved national development area maps for 2007–13 and numerous regional aid regulations.

For aid that targets problems that can occur in all economic sectors or regions (horizontal aid), the Commission has enacted numerous Community frameworks and guidelines, as well as detailed provisions in the GBER.[14]

Small and medium-sized enterprises (SMEs) often have specific difficulties in obtaining capital for start-up, the acquisition of means of production and

intellectual property rights, the recruitment and training of workers or adaptation to environmental standards, or in finding access to new technologies and markets. This is why the GBER allows additional types of aid for SMEs and increased aid intensities (this refers to the value of the aid expressed as a percentage of the total costs that can be aided in a given project).

The Community framework for state aid for research, development and innovation[15] enables the approval of aid intensities graded according to the distance from the market of the different types of research (fundamental research: 100%; industrial research: 80–50%; and experimental research: 60–25%).

The Community guidelines on state aid for environmental protection apply to aid measures which remedy or prevent damage to the natural environment or natural resources, or promote an economic use of these resources.[16]

The Community guidelines on state aid for rescuing and restructuring firms in difficulty concern undertakings that are no longer able to absorb losses, whether with their own financial resources or other resources, which would certainly cause the undertaking to fail in the short or medium term.[17] State aid in favour of such companies can have a particularly distorting effect on merit-based competition and can therefore only be approved under strict conditions (time limitations, and clear restructuring or liquidation plans). The basic rule for both rescue and restructuring aid is that it can only be granted to a company once within a 10-year period (the basic principle of one time–last time aid).

Employment aid can be granted in the context of regional aid or SME aid. In addition, the GBER exempts from obligatory notification labour cost subsidies (within certain limits) for the recruitment of disadvantaged and disabled workers, as well as aid for the additional costs of employing disabled workers. With regard to training aid, the GBER differentiates between specific training measures (with admissible aid intensities of 25–100%) and general training measures (with admissible aid intensities of 60–100%).

Public services (including services of general economic interest and other services of general interest)

First of all, it is important to note that public services that are of a non-economic nature are already exempted from EU competition law (including EU state aid control) because the institutions which provide these services are by definition not undertakings within the meaning of EU competition law. Services of a non-economic nature are, for example, the fulfilment of genuine sovereign tasks, that is, tasks which are per se reserved for the state in the exercise of its sovereign power (e.g. domestic and foreign security, the administration of justice, and foreign relations), and services in connection with the national education system and with social security, for all of which there is compulsory membership and all of which are based on the principle of solidarity. In addition, the activities of trade unions, political parties, churches and religious communities, consumer associations, scientific communities, and charities and aid organisations are normally of a non-economic nature (see the Commission communication *Services of General Interest in Europe*, paragraph 30).[18]

Second, there are also numerous public services or other services and activities that are in the general interest which are of an economic nature, such as the provision of energy, water, transport, telecommunications, post, media, waste disposal, health services and rescue services. The *de minimis* regulation applies to state support in small amounts in these areas. Furthermore, the ECJ declared in its *Altmark Trans*[19] (C-280/00) judgment that compensation, granted by the state regarding the costs of public services and other economic services of general interest, is not aid in the sense of Article 107(1) of the TFEU if

1. the recipient undertaking has truly been entrusted by the state with clearly defined public service obligations;

2. the parameters according to which the compensation is calculated have been objectively and transparently established in advance;

3. the compensation does not exceed what is necessary to cover all or part of the costs incurred in the discharge of the public service obligations, taking into account the relevant receipts and a reasonable profit; and

4. unless the undertaking was selected from a call for tender, that the amount of the compensation is calculated based on an analysis of the costs which an average, well-run undertaking would incur when discharging those public service obligations, taking into account the relevant receipts and a reasonable profit for discharging the obligations.

Third, the Commission decided in November 2005 on a package of three measures (the Monti/Kroes package) that should further improve legal security in the financing of public services. The first measure is a Commission decision,[20] based on Article 106(3) of the TFEU, on the application of Article 106(2) of the TFEU in cases where compensation does not fulfil the *Altmark* test and is therefore aid in the sense of Article 107(1) of the TFEU. The decision has the effect of a block exemption, in that it clarifies the conditions which justify certain compensation systems (essentially a clearly defined mandate to provide public services and no overcompensation) according to Article 106(2) of the TFEU. The Commission does not then need to be notified of these systems. The second measure is a Community framework[21] that clarifies under which conditions public service compensation granted by the state, which does not fulfil the Altmark test and is not included in the aforementioned Commission decision, is compatible with EU state aid law and can be approved after notification to the Commission. The third measure is a reform of the Transparency Directive[22] that extends compulsory separate bookkeeping to undertakings which receive any kind of compensation for the provision of services of general economic interest (whether this is really aid or not) and are active at the same time in other areas of business.

The aid review procedure

The aid review procedure is laid down in Article 108 of the TFEU and the so-called procedural regulation.[23] In all procedures, Member States at

central government level are the only party (and therefore the contact partner for the Commission) that must fulfil the notification obligation, irrespective of whether the aid is to be granted at central state, regional or municipal level.

Member States are obliged, according to the first sentence of Article 108(3) of the TFEU, to notify the Commission of all new aid (including changes to existing aid) before implementation. Exemptions from the mandatory notification apply only to aid which falls under the GBER no. 800/2008/EC,[24] to individual aid granted according to approved aid schemes, and to *de minimis* aid. According to Article 108(3) of the TFEU, a 'standstill obligation' applies until the Commission has reached a decision on the notification; in other words, the aid cannot yet be granted. As soon as the notification is completed, the Commission has a maximum of two months for a preliminary examination in order to decide either

1. that the notified measure does not constitute state aid in the sense of Article 107(1) of the TFEU (no aid decision), or

2. that the aid does not raise any doubts with regard to its compatibility with the internal market (no objections decision), or

3. that such doubts exist and therefore the formal investigation procedure must be opened (opening decision).

The formal investigation procedure is to be concluded within 18 months where possible. At its end, the Commission decides

1. that the notified measure does not constitute state aid (no aid decision); or

2. that the aid is compatible with the internal market and can therefore be approved (positive decision); or

3. that the aid can be approved under certain conditions which would render it compatible with the internal market, if necessary including

obligations to enable compliance with the decision to be monitored (conditional decision); or

4. that the aid is not compatible with the internal market, and is thus prohibited and shall not be put into effect (negative decision).

Any aid granted in violation of the 'standstill obligation' under Article 108(3) of the TFEU (that is, granted without notification or after notification but before the Commission has taken a decision authorising it) is unlawful. There is no time limit for the examination procedure for unlawful aid. During the procedure the Commission can take interim measures to oblige the Member State concerned to suspend the aid, or to provide all the information relevant for the examination or even to demand the recovery of aid which has already been granted. The Commission can take these measures if the aid character of the measure concerned is in no doubt and there is an urgent need to act and a danger of serious and irreparable harm to competitors. Should the examination procedure not end in approval because the aid is not only procedurally unlawful but also materially incompatible with the internal market, the Commission must, according to the procedural regulation, order the Member State to recover from the beneficiary the aid already granted, including interest.

Should the recipient of aid misuse it, in other words use it in breach of the Commission's approval decision (for example, use the aid for another purpose, or contravene an obligation or condition), the Commission can open a formal investigation.

Should the Commission, when examining existing aid schemes according to Article 108(1) of the TFEU, come to the conclusion that an existing measure is not or is no longer compatible with the internal market, it can propose appropriate measures to the Member State for bringing the aid scheme into line with the internal market. These measures can be changes in form and content, the abolition of the aid scheme or even the introduction of procedural requirements.

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Notes

[1] The Lisbon Treaty, which came into force on 1 December 2009, amended the EC Treaty (TEC) and renamed it the Treaty on the Functioning of the European Union (TFEU). Since then, references to Community in the context of the TEC are to be understood as references to Union in the context of the TFEU.

[2] For more information see European Commission, Directorate-General Competition, 'Competition', accessed at http://ec.europa.eu/competition/index_en.html on 20 March 2013.

[3] On activities of a non-economic nature, see below under the heading 'Public services (including other services of general interest)'.

[4] The exception under Article 101(3) of the TFEU applies equally to decisions and categories of decisions by associations of undertakings and to concerted practices and categories of concerted practices. For simplification reasons, all these types of conduct are hereafter summarily referred to as agreements.

[5] Council Regulation (EC) no. 1/2003 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, OJ L1 (16 December 2002), 1.

[6] Although the term concentration is technically the correct one to define all these different forms of lasting change in control, in practice the terms EU merger control and EU Merger Regulation are habitually used to cover all these forms.

[7] Council Regulation (EEC) no. 4064/89 on the control of concentrations between undertakings, OJ L395 (21 December 1989), 1, accessed at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31989R4064:EN:HTML on 20 March 2013;
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[8] For more details see Article 1(1–3) of the EU Merger Regulation.

[9] Commission Regulation (EC) no. 1998/2006 on the application of Articles 87 and 88 of the Treaty to *de minimis* aid, OJ L379 (15 December 2006), 1.

[10] Council Regulation (EC) no. 994/98 on the application of Articles 92 and 93 of the Treaty establishing the European Community to certain categories of horizontal state aid, OJ L142 (7 May 1998), 1.

[11] Commission Regulation (EC) no. 800/2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General block exemption Regulation), OJ L214 (6 August 2008), 1.

[12] NUTS stands for nomenclature of territorial units for statistics
[13] European Commission, *Guidelines on National Regional Aid for 2007-2013*, OJ C54 (4 March 2006), 1.
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Enterprise Policy for Small and Medium-Sized Enterprises

Introduction

Small and medium-sized enterprises (SMEs) are usually referred to as the backbone of the European economy and the driving force for more growth, competitiveness and employment in the EU. A favourable environment in which to begin and establish these enterprises is therefore crucial for Europe. For this reason, in June 2000, the Council of Ministers adopted the Charter for Small Enterprises, which lists 10 key areas for the establishment and development of small businesses:[1]

- education and training for entrepreneurship,
- cheaper and faster start up,
- better legislation and regulation,
- availability of skills,
- improving online access,
- getting more out of the single market,
- taxation and financial matters,
- strengthening the technological capacity of small enterprises,
- making use of successful e-business models and developing top-class small business support, and
- developing stronger, more effective representation of small enterprises' interests at Union and national level.

European policy in recent years has been paying increasing attention to SMEs. In the context of its Europe 2020 strategy for smart, sustainable and

inclusive growth, published on 3 March 2010, the Commission aims to promote successful entrepreneurship by improving the business environment for SMEs so that they may realise their full potential in today's global economy.[2]

Adopted in June 2008, the Small Business Act for Europe (SBA) reflected the Commission's political will to recognise the central role of SMEs in the EU economy and for the first time put into place a comprehensive SME policy framework for the EU and its Member States.[3] The three main objectives were to improve the overall approach to entrepreneurship, to anchor the 'Think Small First' principle in policymaking and to promote the growth of SMEs by tackling their specific problems. The Commission committed itself to the following 10 political principles:[4]

- to create an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded,
- to ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance,
- to design rules according to the 'Think Small First' principle,
- to make public administrations responsive to SMEs' needs,
- to adapt public policy tools to facilitate SMEs' participation in public procurement and better use state aid,
- to facilitate SMEs' access to finance and to develop a legal and business environment supportive of timely payments in commercial transactions,
- to help SMEs benefit more from the opportunities offered by the single market,
- to promote the upgrading of skills in SMEs and all forms of innovation,

- to enable SMEs to turn environmental challenges into opportunities, and

- to encourage and support SMEs to benefit from the growth of markets.

The European Commission has also appointed an SME envoy, whose role is to ensure that the principle of prioritising SMEs' requirements is taken into account in all areas, but especially in law-making.

Another overture has been the creation of an SME portal, an Internet platform which provides access to information on the spectrum of EU policies, legislation, programmes and initiatives relevant to small and medium-sized businesses. Under the heading 'Putting Small Businesses First', the Commission presents a summary of EU SME policies and its central initiatives and programmes.

The European Economic Recovery Plan adopted in November envisaged special measures to support SMEs.[5] These were intended to improve their access to sources of financing. Specific measures have been proposed to reduce administrative burdens and encourage initiative. The 'Factories of the Future' initiative' was one of the three public–private partnership (PPP) options included in the Commission's recovery package. With a budget of €1.2 billion, it supports the manufacturing industry, and especially SMEs, in the development of new and sustainable technologies.[6]

The idea of a European SME week was launched in 2009 to provide information about the support available for SMEs at the European, national, regional and local levels. The aim of this pan-European campaign is to make it easier for existing and potential entrepreneurs to find information, advice, support and ideas to help them develop their businesses.

The economic significance of small and medium-sized enterprises

Definition of the term SME

Member States use the term SME broadly, depending on their own national traditions, so it was necessary to put forward a common definition for use at the European level. An initial definition was recommended on 3 April 1996, stipulating that an SME must have fewer than 250 employees. A recommendation made on 6 May 2003, which came into force on 1 January 2005, revised the definition as follows: [7]

- A business must have fewer than 250 employees to be considered an SME. It may achieve a maximum annual turnover of €50 million and the annual balance sheet total must not be more than €43 million.

- A business with fewer than 50 employees and an annual turnover and/or an annual balance sheet not exceeding €10 million is regarded as a small enterprise.

- A business with fewer than 10 employees and an annual turnover and/or an annual balance sheet not exceeding €2 million is regarded as a micro-enterprise.

The numerical significance of SMEs

In the EU, the typical firm is a micro firm. According to 2010 data, SMEs made up 99.8% of the estimated 20.9 million non-financial business enterprises in the EU27. According to Eurostat, they generated 58.6% of the value added and employed 66.7% of the workforce of the non-financial sector. Moreover, a report published by the European Commission on 16 January 2012 found that 85% of net new jobs in the EU between 2002 and 2010 were created by SMEs.[8] This figure is considerably higher than the 66.7% share of SMEs in total employment. Of the 66.7% share, micro

enterprises contribute about 30%, small enterprises about 20% and medium-sized enterprises about 17%.

As these figures show, SMEs have a huge impact not only on the welfare but also on the economic growth of the EU.

Challenges confronting SMEs

SMEs range from traditional craft workshops to high-tech businesses in the service sector, but they all face common challenges. A European Commission investigation established that SMEs face the following problems: [9]

- bureaucratic and legal constraints,
- problems accessing financial resources,
- taxes,
- shortages of skilled workers,
- difficulties in accessing public procurement contracts,
- unfair competition,
- employment provisions, and
- delayed payments.

Moreover it is noteworthy that, in comparison with the US, a smaller proportion (45%) of the general public in the 27 Member States is interested in starting or heading an SME. In the US the proportion is 61%. Skilled workers for SMEs are thought to be in short supply, but the Commission report points out that SMEs tend to look locally for employees. Of the SMEs questioned, 89% employ staff from their immediate region. In the case of large companies this figure is only 77%.

The Small Business Act: 'Think Small First'

According to the mid-term review of modern SME policy published by the Commission for the period 2005–7, there has been some success in making the economic environment more SME-friendly, both in the Member States and at the EU level.[10] Bureaucratic hurdles have been dismantled and EU funding programmes for the period 2007–13 have been much more clearly structured in favour of SMEs. Despite this progress it was the Commission's view that further-reaching measures ought to be adopted to make better use of SMEs' potential.

The European Commission therefore introduced the SBA on 19 June 2008.[11] The SBA brings together a series of principles and contains a 10-point programme which addresses 92 proposals for specific measures to the Commission and the Member States. In addition, the Commission has proposed specific legislative measures in four areas under the heading 'Putting Small Businesses First—Think Small First'.

The SBA message has been positively received both by Member States and by business organisations. German employers, however, noted that the European Commission still had given no clear statement on the definition of an SME even though one-third of the participants in the Internet consultation on the SBA viewed the lack of a European definition of small and medium-sized enterprises as a problem for their growth. On 11–12 December 2008 the European Council decided in favour of an unrestricted implementation of the action plan adopted on 1 December 2008 in relation to the SBA.[12]

Successful SBA initiatives and ongoing actions

Since the adoption of the SBA in June 2008, European SME policy has made significant progress, especially through actions strengthening SMEs in a number of areas. In February 2011, the commission published an SBA review, reporting on the successful initiatives launched between 2008 and 2010.[13]

The focus of activities between 2008 and 2010 was on initiatives to alleviate administrative burdens, to improve SMEs' access to finance and to support SMEs' market access. Following the SBA review, all legislative initiatives foreseen by the SBA have been adopted, with the exception of the regulation to provide for a Statute for a European Private Company which remains under discussion by the Council.

The creation of such a statute is intended to provide for a uniform type of limited liability company within the EU. Until now businesses have had to found subsidiary companies with different legal formats in each EU Member State in which they wish to do business. This costs time and money. The draft regulation provides for simplification by harmonisation. It contains provisions for the founding of the company, for company shares, share capital, internal organisation, changes of offices and for the restructuring and dissolution of the company. A symbolic amount of one euro is envisaged as the minimum starting capital.

On 23 June 2010, the Council of the European Union approved a new directive on the common system of value added tax (VAT) in regard to the rules on invoicing.[14] Since then, one of the main principles regarding e-invoicing has been the equal treatment of paper and electronic invoices, which is particularly helpful to small businesses.

Businesses with a turnover of less than two million euros may also benefit from an optional cash accounting scheme which makes it possible for them to delay accounting for VAT until they receive payment from their customers.

One of the principles in the SBA for Europe was a reduction in the number of late payments in commercial transactions. In order to help SMEs deal with the problem of late payment, and to assure the proper functioning of the internal market, the directive on combating late payment in commercial transactions was adopted on 12 February 2011.[15] It lays down the specific deadlines for the payment of invoices and establishes a right to compensation in the event of late payment in all commercial transactions,

whether between private and public undertakings, or between undertakings and public authorities. If the date or period for payment is not defined in the contract, the creditor is allowed to charge interest for late payment 30 calendar days after the date of receipt by the debtor. As a general rule, the period for payment fixed in the contract shall not exceed 60 calendar days, unless otherwise expressly agreed in the contract and provided that this is not grossly unfair to the creditor.

Achievements have been made since 2008 in non-legislative areas, too. Ninety per cent of all SMEs have benefited from the Competitiveness and Innovation Framework Programme (CIP) financial instrument so far, and another 200,000 SMEs are expected to benefit by 2013.

The European Investment Bank Group has increased its range of financial products tailored for SMEs, particularly mezzanine finance. In addition, more funds will be made available by the Commission for micro-credit, and access to cross-border venture capital will be easier.

SMEs are often more affected than large companies by European legislation, so the Commission has started to assess all new legislative and administrative proposals at European and national level with regard to their possible impact on SMEs (the 'SME test'). In case of a negative impact, such as overwhelming reporting obligations, Member States shall be able to use measures such as derogations, transition periods or exemptions.

In order to facilitate the provision of feedback on existing or planned regulation, the Commission has established the 'SME envoy'. At present, the envoy is located in the Directorate-General for Enterprise and Industry. His role is to act as an ambassador for the specific interests of SMEs in the EU. He raises awareness of the particular needs and problems which SMEs may have with regard to European regulation. One of his main duties is to promote the reduction of administrative burdens in cases where SMEs may be affected by European regulation. At the same time, a network of SME envoys at the national level was established. The SME envoys are appointed by the national governments and are to promote SMEs' interests within the

national governments and ensure that the 'think small' principle is fully integrated in policymaking on all levels: national, regional and local.

On 23 November 2011 the Commission presented its report *Minimizing Regulatory Burden for SMEs—Adapting EU Regulation to the Needs of Micro-enterprises.*[16] It describes the Commission's new approach to ensuring that the EU is better able to respond to the needs of SMEs. With this initiative the Commission committed itself to exempting micro-enterprises from EU legislation wherever possible or to introducing special options in order to minimise their regulatory burden. The aim of this initiative is to search for exemptions and less intrusive requirements for micro-enterprises both in existing and in new EU legislation. Furthermore the consulting processes for micro-enterprises and other SMEs shall be optimised when reviewing existing EU regulation and preparing new EU laws. The production of annual scoreboards is intended to evaluate the benefits for businesses and ensure a continuing focus on their needs and interests.

Another of the Commission's activities has been the simplification of start-up procedures. In 2000 the European Charter for Small Enterprises included 'cheaper and faster start-up' as one of its 10 action lines. Later, in 2002, the Commission carried out a study on the state of play in the different Member States: the average time needed to start a company in 2001 in the EU15 was 22 days; the cost was €827.

In 2006 the Spring European Council decided to ask Member States to take concrete steps to facilitate start-ups. The conclusions of that Council stated:[17]

> The Member States should establish, by 2007, a one-stop-shop, or arrangements with equivalent effect, for setting up a company in a quick and simple way. Member States should take adequate measures to considerably reduce the average time for setting up a business, especially an SME, with the objective of being able to do this within one week anywhere in the EU by the end of 2007. Start-up

fees should be as low as possible and the recruitment of a first employee should not involve more than one public administration point.

In 2007 and 2008 the first results were available. Times and costs to start a business had been reduced in many countries and one-stop shop's or similar institutions had been established. In 2010 the average time needed to start a private limited company in the EU was seven days; the cost was €399.

In its conclusions in the *'Review of the* '*Small Business Act*' *for Europe'*, the Competitiveness Council on 30 May 2011 encouraged the Member States, where appropriate, to reduce the start-up time for new enterprises to three working days and the cost to €100 by 2012.[18] Moreover, the ministers expressed their wish to limit the time necessary to obtain the needed licences and permits to three months by the end of 2013.

One of the top issues on the Commission's agenda to support SMEs in Europe is to facilitate their access to public procurement. According to the Commission a significant number of barriers discourage SMEs from applying for public procurement contracts. The list includes difficulties in obtaining information, lack of specific knowledge about tender procedures, the large size of the contracts, the cost of preparing the proposal and high administrative burdens. Therefore, the package of directives on public procurement is currently under revision in order to reduce administrative burdens and costs related to tendering, and to make procurement systems more transparent and more easily accessible for SMEs.

The EU is also taking actions to promote standardisation among SMEs. Though there are clear benefits for SMEs in using standards to achieve better market access, cost reduction and new opportunities for product design, SMEs are often not sufficiently represented in the standardisation process. Obstacles to their participation are similar to those in public procurement. Lack of information, high costs, and lengthy and opaque procedures hinder SMEs from taking an active part in the European standardisation process. Standards often are not adapted to SMEs' needs.

To remedy this, the Commission has started a revision of the relevant legislative regulations on European standardisation.

As a consequence of increasing competition from developed and emerging economies, European SME policy seeks to promote international engagement on the part of SMEs. A number of initiatives have been taken, such as the establishment of EU business centres in India and China to help EU SMEs enter these third-country markets. The Intellectual Property Rights (IPR) Help Desk in China has been operational for the past three years and the Enterprise Europe Network continues to grow in third countries.

Moreover, a number of SME policy dialogues have been started—both bilateral (China and Russia) and multilateral (EU–Mediterranean Cooperation and Eastern Partnership). On 9 November 2011 the Commission proposed a strategy entitled '*Small Business, Big World—A New Partnership to Help SMEs Seize Global Opportunities*', which aims to help SMEs expand their businesses outside the EU.[19]

The new strategy sets out six fields of action:

- strengthening and mapping the existing supply of support services,
- creating a single virtual gateway to information for SMEs,
- making support at the EU level more consistent,
- promoting clusters and networks for SME internationalisation,
- rationalising new activities in priority markets, and
- leveraging existing EU external policies.

The aim of the strategy is to bring EU institutions and relevant SME stakeholders closer together and to stimulate a strong partnership with the Member States when taking actions in support of SME internationalisation. A study on the internationalisation of European SMEs was completed in 2010.

Reducing administrative burdens

In order to support the Commission in its action programme for reducing administrative burdens, in August 2007 a high-level group was set up, chaired by the former President of Bavaria, Dr Edmund Stoiber. It has already put forward a series of proposals for the reduction of bureaucracy, especially for SMEs. The proposals, which have been published on the group's Internet site, cover, among other things, the reform of the VAT Directive rules on financial reporting, adopted by the Council on 13 July 2010, and the reduction of administrative burdens in the field of company law.[20]

Under its first mandate the group's main task was to provide advice on administrative burden reduction measures suggested in the context of the *Action Programme for Reducing Administrative Burdens in the EU*, the aim of which is to reduce EU administrative burdens on businesses by 25% by 2012.[21] In the meantime, the Commission has already proposed measures that would reduce bureaucracy by more than 33%, a saving of more than €40 billion. Out of this, the Council and Parliament have already adopted measures amounting to a reduction of 21.8%.

The Commission adopted a new mandate for the high-level group on 17 August 2010. The group will continue its work until summer 2014 to fully exploit the savings potential of the action programme.

On 21 February 2012 Dr Edmund Stoiber handed over the group's report on best practices in Member States to implement EU legislation in the least burdensome way—*Europe can do Better*—which was requested by the Commission in August 2010. The report lists 74 best practice examples including initiatives on e-government, intelligent solutions for small businesses, direct stakeholder involvement, good guidance and cross-border initiatives.[22]

In October 2010 in its Communication *Smart Regulation in the EU* the Commission set out plans to further improve the quality and relevance of EU

legislation.[23] According to the Communication, smart regulation in the future will aim to evaluate the impact of legislation during the whole policy cycle. This means that the costs and benefits of existing legislation will have to undergo a 'fitness check'. The consultation of stakeholders and the quality of impact assessment will be improved. Furthermore, improving the transposition, implementation and enforcement of EU legislation is one of the main issues of smart regulation in the EU.

The most important sources of financing for SMEs

In order to respond to the specific needs of SMEs, the EU offers various financial instruments. Financial support may take the form of grants, loans and in some cases loan guarantees. Support is provided either directly by the Commission or via programmes that are administered on a regional or national basis. Furthermore, SMEs may also take advantage of various non-financial initiatives which provide support to businesses in the form of programmes and services. To offset disparities in regional development, and to promote economic and social cooperation within the EU, the Commission co-finances projects in the Member States by means of the Cohesion Funds.

The European Regional Development Fund (ERDF) is the most important Cohesion Fund in support of SMEs and is intended both to reduce regional developmental imbalances and to promote social and economic cooperation at the European level. Its support covers the financing of a variety of SME-related projects which are designed to strengthen innovation and competitiveness. The goal of this support is also to improve the regional and local parameters for SMEs and to strengthen their inter-regional and cross-border cooperation and their investment in human resources.

Furthermore, the European Social Fund (ESF) supports adaptation to economic and social change. As part of the CIP, €1.13 billion will be set aside from 2007 to 2013 and divided into three programmes.

First, venture capital is to be increased for high-growth and innovative SMEs in their early stages. This will lead to increased leveraging for the support of innovative businesses. Second, the SME guarantee facility provides additional security for an increase in the supply of external financing for SMEs. Market deficits in the areas of access to credit, the availability of micro-credit, access to equity or quasi-equity capital and the securitisation of credit positions can thereby be overcome. Third, a programme for the development of capacities supports financial intermediaries in several Member States. Approximately 110,000 businesses have thus far profited from the programme.

There are also other individual initiatives, such as JEREMIE (Joint European Resources for Micro to Medium Enterprises). This was established by the Commission, the European Investment Fund and the European Investment Bank (EIB) and is intended to improve the access of small and medium-sized businesses to financial resources, in particular to micro-credit, venture capital and guarantees. Particular emphasis is placed on, among other things, the promotion of new businesses and the provision of micro-loans.

JASMINE (Joint Action to Support Micro-finance Institutions in Europe) is an initiative that complements JEREMIE. It is intended to improve access to micro-credit within Europe in two ways: by enhancing the capacities of small financial institutions and the financing of the activities of financial institutions in the non-banking sector. This programme is meant to improve access to otherwise unavailable financial resources for small business owners or the unemployed. The programme was initiated in 2008 for a three-year test phase with €50 million in initial capital.

Beyond this, EIB loans are to support SMEs in the attainment of a solid base of operating capital. The loans may be granted for a period extending from 2 to 12 years. The maximum amount for loans is €12.5 million. These loans are to cover the tangible and intangible investments of SMEs and are granted by intermediary institutions, such as commercial banks.

The European Progress Microfinance Facility of the EU is intended for entrepreneurs and the unemployed who would like to establish a small business. In cooperation with the EIB Group, the starting budget of €200 million is expected to mobilise €500 million in micro-credit.

Simplification of state aid decision-making procedures

The Commission has recognised the decisive role of SMEs in job creation and as a factor in social stability and economic drive. Given difficulties in obtaining capital, risk capital or loans, and given restricted access to information, one of the main goals of the General Block Exemption Regulation (GBER), applicable from 29 August 2008 until 31 December 2013, is to help SMEs by simplifying and better targeting state aid for growth and jobs. The GBER gives automatic approval for 26 aid measures and also exempts certain categories of aid when they are granted in favour of SMEs. Such aid can therefore be exempted from prior notification, saving Member States time in granting aid. In order to help SMEs overcome specific market failures, different types of aid are designed to subsidise SMEs in their different stages of development. The GBER especially allows SME investment and employment aid, consultancy aid and aid for participation in trade fairs.

Forecast: future initiatives in support of SMEs[24]

The Commission views SME policy not as a short-term solution to the current economic and financial crisis, but rather as a long-term strategy for the promotion of intelligent, sustainable and inclusive growth. It is thus intended to continue along the path initiated with the Single Market Act of 2008 and, in future, to advance further legislative and non-legislative initiatives regarding SMEs. Emphasis is to be placed on the further reduction of administrative hurdles, and improved access to financing and international markets, as well as the strengthening of the innovative potential of SMEs. To augment SME

research and innovation, the Commission also plans to increase the participation of SMEs in the context of the new Framework Programme for Research and Innovation for 2014–20, Horizon 2020.

Furthermore, the Commission has presented a proposal for a new programme for the Competitiveness of Enterprises and Small and Medium-sized Enterprises (COSME). With a total budget of €2.5 billion (€1.4 billion for new financial instruments and €1.1 billion for the financing of the Enterprise Europe Network), COSME is to function as a funding programme that continues individual initiatives from the current CIP. The new programme is aimed at SMEs and is intended to improve access to financial resources, as well as to promote entrepreneurship and the establishment of new businesses. The administrative authorities in Member States are also to be supported in their efforts to develop and implement more effective economic reforms.

A central goal of European SME policy in future will also be the promotion of entrepreneurial initiatives. People of all ages are to be encouraged to consider the establishment of an enterprise as a legitimate alternative in terms of their personal career development. In this context, programmes such as Erasmus for Young Entrepreneurs are to provide assistance that will help enable young entrepreneurs to gain cross-border experience and, on the basis of examples of best practices, to receive incentives for the successful establishment or development of a private business. Of further relevance here are specific considerations for family businesses, for skilled trades and micro-enterprises, for migrants as entrepreneurs, for social enterprises and for the promotion of entrepreneurial initiatives from women.

At their meeting in Brussels on 14 September 2011, the European SME envoys agreed that the future priority initiatives of a successful European SME policy should be to create a situation where an enterprise can be established within three days and where SMEs have access to loans. Furthermore, SME appraisals of the development and implementation of new legislative proposals should be taken into account during the impact assessment.[25]

Conclusion

In recent years the Commission has increasingly launched initiatives to address the special interests of SMEs. These have included the dismantling of bureaucratic hurdles and attending to the interests of small and medium-sized enterprises by means of legislative initiatives, financial assistance and setting up funding programmes. These are good approaches, although they are not yet sufficiently well known. They need to be more widely discussed.

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Claus-Peter Schmid

Consumer Protection

Introduction

The term 'consumer protection policy' concerns all safety, economic and legal issues that are relevant to consumers, as well as consumer information and education, and the promotion of consumer associations. Food safety issues must, however, be looked at separately.

Development of the principles of consumer protection

The formation of consumer protection as a separate Community policy is to be viewed against the background of a gradual realisation of the internal market and fundamental freedoms. The interests of consumers were not incorporated into the European Community's founding treaties. The liberalisation of the cross-border traffic of goods and services, brought in with the introduction of basic freedoms, and the ensuing danger to opportune consumer interests, has made it essential to develop a consumer policy at European level as a 'counterbalance'. The introduction of joint, or at least aligned, legislation was meant to break down legal and competitive barriers, thereby helping to create the single market.

The Single European Act (SEA) of 1987 formed the foundation for creating the single market, making consumer protection a component of the Treaty Establishing the European Economic Community (EEC Treaty) for the first time. In the newly created Article 100a, the Commission instigated 'a high level of protection in the areas of health, safety, and environmental protection'.

The Treaty on European Union (TEU)—also known as the Treaty of Maastricht—which entered into force in 1993, accorded greater value to consumer protection, and the influence of this can still be seen in current standards. 'A contribution to the strengthening of consumer protection' was

one of the aims of the Community policy in Article 3(s) of the Treaty Establishing the European Community (TEC). Moreover, under the heading 'Consumer Protection', Article 129a(1) of the TEC states:

The Community shall contribute to the attainment of a high level of consumer protection through:

(a) measures adopted pursuant to Article 100a in the context of the completion of the internal market;

(b) specific action which supports and supplements the policy pursued by the Member States to protect the health, safety and economic interests of consumers and to provide adequate information to consumers.

In the Treaty of Amsterdam (1997) a horizontal clause was added to Article 153 as a key consumer protection standard in the TEC (the consideration of consumer protection in other Community policies), and the scope of its application was extended 'to promote the interests of consumers'. The Treaty of Lisbon retained these provisions in Article 169 of the Treaty on the Functioning of the European Union (TFEU).

Prevailing legal position

According to the current legal position, the Community contributes to 'protecting the health, safety and economic interests of consumers, as well as to promoting their right to information, education and to organise themselves in order to safeguard their interests'.[1] These aims are to be seen as matters to be weighed up when establishing and executing other Community policies and measures.

Article 169 of the TFEU enables the Community to make consumer protection a priority aim of any measures to be carried out. This

competence is in any case restricted to supporting, complementing and monitoring the policies of Member States and may not take the place of each Member State's consumer protection policy. The Commission, however, has extensive competence for making regulations, in accordance with Article 114(3) of the TFEU, for single market–related consumer protection policy (legal alignment measures), where the aims of consumer policy are not at the forefront. The Commission is, in accordance with Article 114(3), bound to provide a high level of protection in its proposals for laws on consumer protection and must 'in particular take into consideration all new developments based on scientific results'.

Indeed, the consumer is mentioned several times in the TFEU, but is not defined. Nor does secondary legislation contain uniform terminology to describe the consumer. There is, however, at least a consensus that purchasers and users of all types of commercial services for private use are included under the term of consumer, and that consumers are defined more in terms of the role they play in the single market than in terms of their need for protection.

Consumers should, in principle, be able to look after their own interests and make well-founded purchasing decisions. To do this, they need to have accurate information and be entitled to legal recourse if a deal goes wrong. The purpose of the Community measures must therefore be to balance out the structural imbalances between individual consumers and companies that come about because consumers are in an economically weaker position, and because it is more difficult for them to obtain information and to get legal advice.

In some cases, creating a basis for rational purchasing decisions and legal recourse is not enough to protect the consumer, particularly in health and safety matters. In such cases, harmonised legislation is needed to guarantee all consumers' appropriate protection.

The purpose of EU consumer policy

EU consumer policy should provide fundamental health protection and safety precautions and protect the economic interests of all EU citizens, who expect a high level of protection. Products and services that are placed on the market must be safe. The EU is involved in both legislation and other measures that have an immediate effect on market behaviour, such as the creation of standards, corporate codes of conduct and optimum procedures.

It is important that consumers have comparable opportunities to make full use of the potential of the single market—broader choice, lower prices, affordability and the availability of basic services. Barriers to cross-border trade should be removed so that the consumer dimension of the single market can develop in parallel to the company dimension. EU consumer policy aims to create a coherent and uniform environment throughout the whole of the EU, so that consumers can make purchases outside of their home country without worry.

For consumers, it is not only specific consumer rights that are of importance; their rights are affected by other important policy areas in the EU, such as the single market, trade, financial services, competition and so on. Consumer policy cannot, therefore, operate in isolation.

The creation of a Directorate-General for Health and Consumers and the restructuring of scientific and legislative work prove that the Commission is according ever greater importance to consumer policy. In line with this, in 2007 a commissioner was appointed to be solely responsible for consumer protection for the first time.

Planning and financial support for EU consumer policy

The Commission lays down directives for the future structure of consumer protection through non-binding programmes and recommendations lasting

several years. The consumer protection action programme initiated in 1975 and lasting until 1981 was of particular significance in policy terms. It laid down the aims—which still play a decisive role today—for health, safety, economic interests, compensation, education and information, as well as the collective representation of interests.

The consumer policy strategy for 2002–6 pursued the following objectives:[2]

- an equally high level of consumer protection,
- effective implementation of consumer protection legislation, and
- the appropriate incorporation of consumer protection policy.

For the first time, this strategy contains the beginnings of full harmonisation, whereby legislative provisions should leave no room within their area of application for other provisions at the national level, which will further improve the single market and protect the consumer.

The consumer policy strategy for 2007–13 follows on from previous programmes. From a financial perspective, it is flanked by the Programme of Community Action in the Field of Consumer Policy (2007-2013).[3] This programme has provided around €157 million of financial assistance in total from the Community (a financial share from the Community of 50%–95%) for the lifetime of the current financial framework.

The consumer policy strategy for 2007–13

The consumer policy strategy for 2007–13 is supported by two central ideas: a contribution to growth and employment (the Lisbon Strategy) and greater proximity to the citizens.

The 493 million consumers in the EU are crucial for the economy because their purchases represent 58% of its gross domestic product. Well-informed consumers act as drivers for economic change. Their decisions drive innovation and efficiency forwards. In their role as consumers, citizens can experience direct contact with the EU and the advantages of the Community.

The Commission has expressed three main aims:

- To strengthen consumers: the consumer should be equipped with decision-making skills so that he or she can play a full role in the market, and transparent markets, accurate information, effective protection and firmly anchored rights should be guaranteed for mature consumers;

- The improvement of consumers' well-being in terms of price, quality, affordability and safety, as these are the signs of correctly operating markets; and

- The effective protection of consumers from serious risks and dangers where they are not able to fend for themselves.

The overriding aim is to bring about a more comprehensive and more effective single market by 2013, particularly in the retail trade. Consumer markets should be competitive, open and fair to ensure the cross-border trade of safe products and services. The social and economic integration of consumers should be guaranteed by ensuring that consumers have access to fundamental services at affordable prices. All individual traders, in particular small and medium-sized enterprises (SMEs), should be able to sell anywhere in the Community on the basis of uniform, uncomplicated regulations.

The Commission is also seeking to achieve greater coordination between EU consumer policy and other areas of EU policy. Collaboration between Member States should be intensified.

Key functions of the EU strategy

Retail trade and the single market

The single market is still far from being a comprehensive EU single trade market. This is denoted by its fragmentation into 27 national single markets. The prospects for extending the single market are good because in an increasing number of economic areas, such as air traffic and the music market, there are no technological barriers to expansion. As cross-border shopping develops as an alternative to what is on offer on the national markets, consumers will have greater choice, and on national markets, there will be greater competition.

Cross-border retail trade has, however, made no headway. The percentage of consumers who made a cross-border purchase in 2008 was more or less the same as for 2006, at 25%. Forty-nine per cent of retail traders (and 33% of consumers) would be prepared to trade across borders (i.e. make purchases) if consumer protection provisions were harmonised across the EU.[4] This proves that the EU retail trade single market has huge potential.

Hindrances to an independent retail trade single market are due—in addition to linguistic barriers and logistical problems—to differences in shipment and payment systems, as well as to a lack of consumer trust and to regulatory obstacles. Consumer protection standards are different in each Member State. This lack of homogeneity is reflected in the differing levels of trust that consumers have in existing consumer protection standards. The percentage of consumers who consider themselves to be sufficiently protected varies from 13% (in Bulgaria) to 74% (in the Netherlands).[5]

Technological change (electronics)

Technological change is moving ever more quickly thanks to the Internet and digitalisation. The increasing popularity of electronic trade as a sales channel is reflected in the increase in sales made via the Internet. In 2008,

31% of consumers bought at least one item over the Internet, compared with 27% in 2006. In the Nordic countries, the percentage of services and products bought over the Internet in 2008 equalled 91%.[6]

An increasing number of consumers and retail traders in the EU are aware of the advantages that electronic trade offers them. Electronic trade increases the size of the market they move in and gives them access to more suppliers. Traditional advertising and sales methods via traditional consumer markets are coming under increasing pressure. This raises the question of whether traditional consumer rights should be adjusted to bring them more into line with the digital age.

The social dimension (an increase in the number of consumers requiring protection)

Internet trade and digitalisation are salient examples of the extended trade framework that mature consumers now have. With a greater number of opportunities comes a greater level of personal responsibility. Most consumers make the most of these opportunities. Children and older people, as the weakest groups in society, are unable to do this and, as consumption levels rise, they need special protection. It is important that consumer protection policy ensures that these groups can take advantage of these market conditions while being aware of their responsibilities.

The increasing importance of the service sector

The service sector has grown in recent years compared to the manufacturing industry. The variety of liberalised services should increase further with the liberalisation of the electricity, gas, postal and telecommunications sectors. The progress made in these areas should bring advantages for the consumer (greater choice and better offers, etc.), but at the same time, this transition places new challenges in the path of the consumer (i.e. too much choice, opaque pricing structures, etc.). The legislator must therefore ensure that the changes taking place in the economic trade environment serve the interests of the consumer.

Putting the political aims of the consumer policy strategy into practice for 2007–13

Better monitoring of consumer markets and national consumer policies

Through better monitoring of consumer markets, areas where the single market is not working from a consumer perspective ('market disturbance') should be identified. Key indicators for the screening of consumer markets are consumer complaints, price levels, consumer satisfaction, the ability to change suppliers and product safety. The Commission will supplement these indicators with investigations into the integration of single trade markets and the systematic benchmarking of individual Member States on their success in enforcing these measures and making redress mechanisms available for consumer protection.

In 2009, the Commission put forward the Consumer Barometer as an instrument geared towards meeting these demands. The Commission came to the conclusion that basic services in the areas of transport (bus and rail), energy provision (electricity and gas) and the banking system pose the greatest problems for consumers. The Commission believes that this instrument can be improved and is endeavouring to generate a more comprehensive level of consumer data by working more closely with Eurostat and the national authorities. The Seventh Framework Programme for Research, Technological Development and Demonstration should also provide reliable findings on consumer behaviour, and research into this area should be set up as an autonomous branch of research.

Better consumer protection regulations

The Commission's Green Paper *The Review of the Consumer Acquis* [7] sparked off a discussion whose aim was to simplify, complete and modernise the existing legal framework. The review aimed to come up with eight directives for consumer protection. The top priority was to achieve a real single market with, to the greatest possible extent, 'the right balance between a high level of

consumer protection and the competitiveness of enterprises, while ensuring the strict respect of the principle of subsidiarity.'[8] Consumers should be able to call upon the same rights anywhere within the EU. SMEs in particular should be able to benefit from simplified regulations and should not be prevented from trading throughout the EU because of the excessive expenditure required to comply with consumer laws and regulations.

Current consumer law is predominantly characterised by provisions that include solutions to consumer protection issues in specific areas. Fundamental principles that span different sectors are, for the most part, not pursued in the existing set of regulations. Diverging regulations (e.g. different cooling-off periods for cancellation rights) have been created, in some cases for comparable issues. The result is a lack of stringency and contradictions in European consumer protection law. In addition, the principle that holds sway—that most EU consumer protection provisions provide for only a minimum level of harmonisation—has led to considerable fragmentation of the law. Member States are permitted to pass stricter provisions when harmonising their laws with European laws. The Commission has confined the legitimacy of this approach to the past. In the time of the digital revolution and the need for a smoothly operating single market, it sees differing national provisions as a barrier.

Given the need for regulation, the Commission is in favour of the total harmonisation of consumer regulations to a sufficiently high level of protection. Bringing protection down to the lowest common denominator should be avoided. The Commission prefers a horizontal approach that governs the joint characteristics of consumer protection in one or several framework regulations (e.g. the term 'consumer'), and, alongside this, enables certain vertical measures in some cases (the revision of some current directives) as a strategic approach to improve the *acquis* of consumer law.

The fundamental discussion about the scope of a horizontal instrument—whether it be a comprehensive, common legal foundation, or merely to aim for the 'common denominator' of joint regulations from various directives—has not yet been decided.

Consumer law provisions that have been passed

European Parliament and Council Regulation (EC) no. 593/2008, passed in 2008 on the law applicable to contractual obligations (Rome I),[9] provided for special separate regulations in favour of the structurally weaker consumer. The Rome I Regulation enables contracting parties to choose the applicable law. If no agreement is made, consumer law is applied for consumer agreements, but with agreements between business partners the place where the service was carried out determines the applicable law. The regulations for consumer agreements were disputed right to the end. The Commission's original idea was not to allow the choice of applicable law. For SMEs this would have meant complying with the legal provisions of all the 27 Member States if the company wanted to sell its products via the Internet, because the consumer law of the home country of the consumer would have been the decisive factor. To ensure a balance between company contractual freedom and the interests of the consumer, it was therefore important for small companies to continue to use their own terms and conditions as the basis for the agreement. The consumer is then also protected because the mandatory consumer provisions of national law are not optional.

The recently adopted Consumer Credit Directive[10] and the extended Timesharing Directive[11] are the result of the harmonisation principle. Both directives include concluding regulations for the legislation of Member States. The Consumer Credit Directive makes it possible for offers of credit thanks to be compared using uniform transparency rules and for annual percentage rates to be calculated using the same methods. The area of application for the Timesharing Directive now also includes short-term agreements for usufruct of holiday property (for a term of less than three years), agreements on mobile items (house boats, campervans, etc.), and provisions for resale and exchange.

The proposal for a directive on consumer rights[12]

As a result of the review of the Community *acquis*, in October 2008 the Commission put forward a proposal for a directive on the rights of

consumers. Four consumer protection directives should be brought together to form a regulatory instrument.

A comprehensive, horizontal reorganisation of consumer contract law has not yet taken place. The aim of the proposal is to improve the ability of the single market to function through strengthening consumer confidence and encouraging companies to participate in cross-border trade (in particular via the Internet). In order to keep the costs of complying with fragmented consumer law down, the minimum harmonisation concept behind the directives that has been adopted until now will give way to full harmonisation. The draft provides for regulations on the pre-contractual obligations of traders to provide information, delivery and risk transfer, cancellation and guarantee rights, abuse clauses in contracts, Internet sales, and Internet auctions.

Members of the European Parliament (MEPs) expressed criticism of full harmonisation at the first reading at the meeting of the committee with overall responsibility for the single market and consumer protection. MEP Andreas Schwab (European People's Party/Germany) argued in favour of proper alignment as a way of providing opportunities for SMEs to increase their exports because the pressure to settle in other Member States should reduce. Changes to the planned catalogue of abuse clauses should not, however, be included in the comitology procedure. During the policy debate in the Competition Council, the need for testing was expressed from many sides due to the unclear effects of full harmonisation.

Better implementation of the law and better legal protection

Continuity of the enforcement actions

Enforcement actions were a key part of the previous strategy. This led to the pioneering Regulation (EC) no. 2006/2004[13] on cooperation in consumer protection for cross-border (official) legal enforcement. The ensuing network of national consumer authorities (NCA) responsible for enforcing consumer law in Member States, as well as in Norway and Iceland, ceased activity in 2007 and an investigation (of misleading advertising and illegal practices) into flight ticket

offers on the Internet (an 'EU sweep') was carried out under the coordination of the Commission in 15 Member States. Great store is also set by correctly implementing the Unfair Commercial Practices Directive 2005/29/EC[14] as well as by monitoring product safety. RAPEX[15], the early-warning system set up by the EU for dangerous consumer goods, should also be extended.

Collective enforcement of consumer law

The discussion about the introduction of instruments for collective enforcement of consumer law at Community level is starting to take a prominent position. The *White Paper on Damages Actions for Breach of the EC Antitrust Rules*,[16] put forward in 2008, marked the beginning of this. A Green Paper on collective enforcement procedures for consumers[17] addressed the consumer-specific aspects of this issue, also in 2008. The expansion of markets means that if an individual trader breaches consumer rights, a large number of consumers are bound to be affected. The Green Paper therefore proposes mechanisms for collective consumer redress and aims to develop effective instruments for this for the whole of the EU. At the same time, companies will be protected from unjustified claims, punitive damages and excessive costs through safeguards.

The Commission considers high legal costs, complex procedures and ignorance of the redress methods available as the reasons for individual consumers rarely taking legal action against unfair business conduct. The smaller the claim, the less likely it is that legal action will be taken. There are now various forms of collective redress procedures in place in 13 Member States. Insufficient financial support and a lack of expertise on the part of consumer organisations are seen as hindrances to the efficiency of existing collective procedures.

In order to improve consumer protection that is deemed to be unsatisfactory, the Commission put forward for discussion four options for action, graded by their level of harmonisation. These range in scope from the proposal not to adopt any new EU measures, via forms of strengthened cooperation between Member States (the expansion of existing collective

legal procedures and their introduction in states that do not yet have any) and a combination of instruments, to the uniform introduction of collective legal proceedings and binding or non-binding EU measures. The penultimate proposal in particular sparked off a broad and open discussion, during which concerns were articulated that some elements of the US legal system (US class actions and the lawsuit industry) could find their way into the European legal system.

To avoid such developments, the Commission is considering the ideas of certifying the representatives of consumer interests and compelling the defeated party to bear the costs of the legal action. Success fees should not be allowed. The financial risks of collective legal actions for the consumer might be lessened through a decree on legal fees, the limitation of legal costs, the financing of lawsuits by associations with public funds, and the 'sharing' of any compensation awarded by consumer organisations should the case be successful. Group actions would be conceivable in a form where consumers opt into an action, and where consumers not willing to take part in the action must deliberately opt out of the group taking legal action.

The plenum of the European Parliament, in its resolution on the *White Paper on Damages Actions for Breach of the EC Antitrust Rules*[18] on 26 March 2009, came out against group actions based on the US model, punitive damage payments and opt-out solutions.

Conclusion

For the first time, with its consumer policy strategy for 2007–13, the Commission is taking a comprehensive approach to consumer policy in the conceptual orientation of its legislative activity. Until now, Community consumer policy has been characterised more in terms of finding solutions for consumer policy issues and has therefore largely been restricted to sector-specific consumer protection regulations.

The *Green Paper on the Review of the Consumer* Acquis[19] and the ensuing draft directives on the rights of consumers (relating to the substantive law side of consumer protection), as well as the *Green Paper on Consumer Collective Redress*[20] (the legal procedure side), are an expression of the new understanding and desired form of organisation that have been brought about by the correct functioning of the single market. Both leading projects of the consumer policy strategy are based on the principle of full harmonisation. This inevitably leads to conflicts with current ideas in national regulations, which often incorporate a greater level of consumer protection in accordance with the principle of minimum harmonisation, and are often based on traditional, national institutes operating under private law. The struggle to manage these opposing respective interests appropriately is likely to dominate consumer policy debate in the coming years.

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The Transportation Policy of the EU: The Next Decade

Introduction

Securing and promoting ever-increasing mobility are important factors for a contemporary transportation policy. The significance of this mobility, that is, the free movement of persons and goods, is even made clear in the name of the directorate-general (DG) of the Commission responsible for mobility and traffic, 'Move'. The DG was created in 2010, when the former DG Traffic and Energy (TREN) was divided into two. The independent management structure is additional evidence of the important political role that the issues of mobility and transport have on a European level. Furthermore, transportation is one of the policy areas that is most strongly regulated at the European level.

Legally established in the Treaty of Lisbon, DG Move is responsible for all modes of transportation: air, road, rail and water (lake and internal shipping traffic). DG Move serves, therefore, to further the completion of the internal market. It also serves to secure ongoing development, to promote better territorial cohesion and integrated land-use planning (through the construction of larger traffic networks in Europe, for example), as well as to control airspace, increase security and expand international cooperation.

The Lisbon Treaty did not open a new legal chapter in the field of transportation policy. The current legal foundation can be found in Article 4(2)(g) of the Treaty on the Functioning of the European Union (TFEU). Transportation and trans-European networks are part of the 'shared competences', which means that the Member States maintain their right only for as long as the EU—in view of the principle of subsidiarity—does not exercise its competence.[1] In the TFEU transportation policy was transferred completely to the area of qualified majority voting (the co-decision procedure in the area of transportation had already been introduced in the Treaty of Amsterdam). According to Article 58(1) of the

TFEU, the provisions of Articles 90 to 100 govern the freedom to provide services in the field of transport. Articles 90 to 100(1) of the TFEU apply to roads, rail and internal ship transportation (the 'modes of internal transport'). For sea and air transportation (the 'globally operating transport services'), the special provision of Article 100(2) of the TFEU applies. In this area the European Parliament and Council can enact 'appropriate provisions' (secondary provisions) in accordance with the ordinary legislative procedure.

More than two-thirds of the legislation in the Member States dealing with transport has since been based on European requirements. However, legislation passed on the European level that will affect the transport sector is not based exclusively on legislative proposals brought forward under the auspices of DG Move. Initiatives that affect the transport sector have also been proposed by DG Environment (e.g. emissions targets), DG Enterprise and Industry (e.g. legal requirements for technical harmonisation), DG Taxation and Customs Union (e.g. to harmonise consumption taxes on energy), and DG Internal Market and Services (e.g. cross-border permits for transport trucks).

The guiding political authority for any action in the area of transportation, for the Commission, as well as for DG Move, remains, as in the past for DG Transportation and Energy, the latest White Paper.

The Commission released its first White Paper, *The Future Development of Common Transport Policy,* in December 1992.[2] The key then was to open up the transport market. Dismantling the barriers to the cross-border movement of goods and services between the Member States was the key goal. The White Paper laid the groundwork for the creation of an integrated European-wide transportation system.

The wide-ranging opening up of the market in the last few decades to owner-operated transport trucks has dramatically increased the efficiency of the various transport suppliers, both in terms of speed and comfort and in terms of their security.[3] Since then, as a result, a higher degree of mobility has been secured and this could be further expanded.

Since the release by the Commission of the second White Paper in 2001, entitled *European Transport Policy for 2010: Time to Decide,*[4] European transportation policies have moved more strongly in the direction of a harmonised and coherent use of the various transportation options, that is, towards them being better connected and interlocking ('co-modality'). The development of European transportation policy has also been strongly influenced by other economic factors, such as increasing globalisation and rising energy costs. The obligations of international treaties have also played a role, such as the need to take account of environmental aspects within the context of the overall transport sector because of the Kyoto protocol. These factors led the Commission to take stock on an interim basis of the results of its 2001 White Paper and to release its 22 June 2006 Communication, *Keep Europe Moving: Sustainability for Our Continent.*[5] The goal of the Communication was to base future European transportation policies on the changed framework conditions. The reorientation was needed because the Commission had come to the view that the measures previously introduced were not sufficient to attain the desired goals by 2010. For this reason the language of a modification of the transportation policies of 2001 is used. A primary goal in 2001 had been to move as much cargo transport as possible via rail and the Commission has not disassociated itself from this position. The Commission has also set the goal, among others, of improving the interoperability of the transportation networks, as well as taking measures to improve sustainability.

Many of the action plans and Communications from the Commission in the following years were connected to this new orientation, for example, the Freight Transport Logistics Action Plan of 2007,[6] as well as concrete legislative initiatives such as the proposed regulation on CO_2 emissions from new transport trucks,[7] or the proposal for a directive to allocate 'external costs' to transport trucks,[8] which came into effect in October 2011[9] after the European Parliament and Commission finally agreed on a compromise (on this see also the section entitled 'Road transport').

The Transport White Paper: Directions for Transport Policies until 2050

With its 28 March 2011 White Paper, *Roadmap to a Single European Transport Area: Towards a Competitive and Resource Efficient Transport System,*[10] the Commission laid the groundwork for European transport policy until 2050 and outlined its vision for the future as well as the key measures needed, in its view, to reach that vision.

Goals and challenges according to the Commission

In the transport White Paper the Commission describes a well-functioning transport system as the heart of the European internal market and territorial and social cohesion in Europe. It has a direct impact on the quality of life of European citizens and makes economic growth and the creation of new jobs possible. In the face of new challenges, however, the transport system stands at a crossroads. This means finding a way to bridge the gulf between the growing demand for mobility from 500 million European citizens with the environmental and climate protection goals of the EU. In the spirit of the flagship initiative of the Europe 2020 strategy, *A Resource Efficient Europe*,[11] the Commission wishes to install a high-quality mobility system that will support economic progress, increase Europe's competitiveness and allocate resources more efficiently and at a lower cost. In all these ways the transport White Paper is closely connected to the Communication released on 8 March 2011, *A Roadmap for Moving to a Competitive Low Carbon Economy in 2050.*[12]

The primary concern of the Commission with respect to the European transport policies of the future described in the transport White Paper is that less and cleaner energy be used, that more modern infrastructure be built, and that the negative impact of transport on the environment be reduced. In the White Paper the Commission envisions a new transport system in which much more freight and many more passengers are moved together to their destinations by the most efficient transport carriers possible. Single-user

transport would take place primarily over the 'last mile', in clean vehicles. Modern information technology would make more reliable information regarding the most efficient transport options available more quickly. The contribution of all users of transport to the total costs of transport would result in revenue that could be used to reinvest in the transport system, thereby reducing traffic jams and other forms of gridlock, and making better systems of information, better services and greater security possible. The transport system would rely on all transport providers using energy efficient vehicles and optimal logistics, and the introduction of modern transport information systems, such as the Integrated Transport System (ITS), the Single European Sky ATM Research Programme (SESAR) and the European Railway Traffic Management System (ERTMS), as well as the opening up of the transport market (e.g. the complete development of an integrated European rail market). The final remaining restrictions to cabotage[13] would be removed and intelligent pricing and tax systems would be introduced across Europe.

At the centre of the Commission's concern is mobility over medium and longer distances, as well as within inner cities. It is for medium-distance journeys that new technologies are needed. New drive technologies and cleaner fuels will not be enough to solve the problem of congestion. For this reason, the introduction of more buses is as necessary as the development of multimodal mobility solutions that make use of rail and air traffic.

Airports, ports, and train, metro and bus stations should be better connected in the future. In the same way, all transport users should make much greater use of online booking systems. Because freight transport over distances of less than 300 kilometres will largely continue to take place by road, improvements in energy efficiency and the increased use of biofuels by transport trucks are urgently needed. Over longer distances, a more efficient use of co-modality and the optimisation of freight corridors need to be achieved. More investment is needed to improve the capacity of the rail network.

In relation to transport across longer distances and international transport, the capacity of European airports is to be expanded to meet the

greater demand for mobility from and into third countries (see below). The European aircraft industry must be a leader in developing fuels that result in reduced CO_2 emissions. There is to be an investigation into market access for ground traffic services to European airports.

In order to respond to the transportation policy challenges by 2050, it will be necessary to take into account social and economic trends. Among these are increasing CO_2 emissions and the continuing dependence on oil, as well as the increasing demand for mobility among European citizens in the context of the achievement of the internal market. In September 2009, the Commission released its Communication, *A Sustainable Future for Transport: Towards an Integrated, Technology-Led and User Friendly System*[14] to prepare the way for the coming transport White Paper. It makes the reduction in greenhouse gases the core element of future European transport policy, because the fact remains that 96% of the energy used for transport comes from fossil fuels. The cornerstones that will orient the realignment of Europe's future transport policy include the following elements: population ageing, migration and movement into inner cities (urban intensification), environmental aspects (CO_2-reduction targets, emissions-trading etc.), the implementation of sustainability through an increase in road safety and the quality of transport, the installation of a fully integrated transport system, the creation of key positions in research and technology, strengthening competitiveness, a lean management structure, and targeted support for education and training, as well as effective administration at all levels.

The recommendations of the Commission are aimed first of all at progressively freeing Europe from its dependence on oil without harming either mobility or the capacity of the transport system to function. The global shortage of oil and increasing demand means that the price of oil has become volatile and unpredictable. Moreover, the EU has signed international agreements to work towards the goal of keeping the increase in the earth's temperature to less than two degrees Celsius. To do so, the EU must reduce its CO_2 emissions by 80%–95% of the 1990 level by 2050, as it has promised to do in *A Roadmap for Moving to a Competitive Low-Carbon*

Economy in 2050 (see above). This will require reducing CO_2 emissions produced by transport by 60%, despite an expected increase in freight transport of 80% and an increase in private transport of 51%. The problem of congestion on the streets of Europe and in air travel will need to be tackled as well. In order to make the most efficient mobility possible within the internal market, the differences in the quality of the transport infrastructure between Eastern and Western Europe will need to be addressed. In its deliberations, the Commission begins with the assumption that volumes of traffic cannot continue to increase at the current rate. The transportation of goods will increase by an estimated 40% above 2005 levels by 2030 and by 80% by 2050. The volume of individual private traffic will increase by 34% by 2030 and by more than 50% by 2050.

Without changes to the system, any increase in traffic will, in the first place, greatly overburden the roads. Above all, however, an additional increase in CO_2 emissions would lead to an even greater increase in global temperatures. For this reason it is essential, in the Commission's view, to keep the harmful consequences of traffic in check. The Commission does not see any restrictions on mobility, especially human mobility, as a solution to the problem.

The Commission responded to the changing social and economic challenges by developing a long-term strategy, the goal of which is to ensure the sustainability of the EU's transport system by 2050. The transport policy strategy of the EU is embedded in the goals of the Europe 2020 strategy for growth and employment. It is therefore closely bound up with other EU policies such as the environmental, economic and regional policies, as well as consumer protection. The Commission is of the view that transformation of the transport sector should be comprehensive, including every level of the common European transport area. The transformation should include modernising technology, changing the behaviour of those who use transport, and improving transport infrastructure and its financing, as well as the international dimension of European transport policies. Every legislative initiative originating in the transport White Paper must include an impact assessment, especially with a view to the European value added, while also taking subsidiarity aspects into account.

According to the Commission, the future conception of the European transport system must be based, above all, on a broad coherence between measures taken at the European level and those taken at the level of the Member States. A scenario in which, for example, only one Member State moves to introduce electric vehicles while another Member State moves to introduce bio-fuels would be counterproductive for European mobility.

The Commission wants to ensure that the measures it takes will improve the competitiveness of the transport sector and at the same time create a reduction of at least 60% in the greenhouse gas emissions produced by transport, as required by 2050. Therefore the recommendations it makes in the future will be oriented to the following 10 goals, which can be regarded as guiding values:

- reducing by half the number of transport trucks powered by conventional fuel by 2030, with complete elimination by 2050;
- ensuring that 40% of the content of aircraft fuel should emit less CO_2 by 2050 and that CO_2 emissions from ships should be reduced by at least 40%;
- ensuring that at least 50% of all passenger and freight transport over a distance of greater than 300 kilometres is by rail or ship;
- the completion of the European high-speed rail track by 2050. A three-fold increase in the current network by 2030, and the maintenance of a high-density rail network;
- the establishment of an EU-wide multimodal Trans-European Transport Network (TEN-T core network);
- the connection of all airports to the rail network, especially to the high-speed rail network, and the connection of all ports to the freight rail network;

- the completion of a common European airspace. The introduction of an air-traffic management infrastructure, a management system for land and sea transport and the satellite navigation system, Galileo;

- the creation of a European multimodal traffic information, management and payment system;

- a reduction in the number of deaths caused by traffic accidents to as close to zero as possible; the EU aims to be the global leader in technological security and danger avoidance in all means of transport; and

- a reversal of the contributor or user principle in terms of costs, and greater participation by the private sector in transport.

In addition to these 10 guiding values that are intended to bring about a reduction of 60% of greenhouse gases caused by transport by 2050, the Commission has released a list of 40 initiatives, each complemented and supported by concrete measures. A whole range of these initiatives will apply to all or almost all transport providers. Among these are plans for urban mobility, for the trans-European traffic networks in the broadest sense and, above all, for the planning and financing of these networks (especially the inclusion of private businesses in the financing of the infrastructure) and the ongoing internalisation of external costs. In addition, plans are to be presented in the areas of research and innovation, as well as electro-mobility. The Commission has also announced additional measures in the areas of passenger rights and traffic safety, including the transport of hazardous goods, as well as for the conditions of employment and work in the transport sector.

Since cities are the most affected by congestion, poor air quality and noise pollution, a gradual phasing-out of vehicles powered by conventional fuels is an important target.[15] For this goal to be achieved, new drive systems will need to be developed and supported by a suitable new refuelling infrastructure that utilises bio-fuels. Mass transit must be promoted

in the cities, as should smaller, lighter vehicles designed specifically for city traffic. Greater use must be made of electric, hydrogen and hybrid vehicles in order to meet this goal.

The themes of 'urban mobility' and 'local transport' belong here too. In the context of the mid-term assessment of the 2001 White Paper mentioned above, the Commission had already given notice of its intention to take up the issue of local transport and especially the concept of urban mobility. After many consultations, on 30 September 2009 the Commission presented an action plan for urban mobility. The 20 measures proposed in the action plan are divided into 6 areas and have the goal of supporting local, regional and national authorities in their efforts to realise an ongoing increase in mobility in cities. For 2012 the Commission has announced that it will take stock and evaluate the need for additional measures. According to data compiled by the Commission, congestion, accidents, air pollution and wasted energy are a burden on the European economy and detrimental to the health of the citizens of Europe. More than 70% of the population of the EU lives in urban areas and approximately 85% of gross domestic product is produced in cities. It is estimated that 40% of CO_2 emissions and 70% of other harmful emissions produced by traffic on the streets are the result of city traffic. One-third of all traffic accidents that result in a fatality take place in an urban area.

The position of the European Parliament

The European Parliament (EP) had already received the report *A Sustainable Future for Transport* in July 2010[16] in order that it might have some influence on the Commission's future White Paper. At the centre of the report was the efficient co-modality of all transport providers; a deliberate shift in transport from roads to rail was rejected, but an increase in the efficiency of all transport providers was supported. The cornerstones of this report are the de-carbonisation of transport, the promotion of research and the development of sustainable and environmentally friendly transport technologies, the internalisation of external costs for all transport providers, the promotion of safety for all active and passive participants in transport, the implementation of a road transport agency to improve road safety, the

creation of a transport fund, and the recommendation that a study be carried out on the consequences of speed limits. The EP urged the adoption of measurable goals such as the reduction of the number of traffic fatalities and the seriously injured in road accidents by 40%, as well as doubling the numbers of those who use buses and rail for transit within cities by 2020.[17]

In response to the transport White Paper of 28 March 2011, on 15 December 2011 the EP adopted the Grosch Report.[18] A large majority of the Members of the European Parliament demanded the adoption of legally binding targets for reductions in the greenhouse gases produced by the transport sector, targets that would be applied within this decade. Whereas the Commission only sought a reduction of 20% by 2030 in CO_2 emissions compared with the level of 2008, the Grosch Report demanded that this reduction be achieved by 2020. In addition, by 2014 the Commission is supposed to present a plan showing how the external costs of all transport providers will be included in the total costs. The goal of this request is to end the handicaps faced by environmentally friendly transport providers. The EP welcomed the White Paper in principle, but insisted that there be concrete measures and a series of goals on the way to reaching the final goal of a 60% reduction in CO_2 emissions from the transport sector by 2050. The EP demanded, for example, that mega-trucks be permitted only if requested by individual Member States and only on certain roads where the infrastructure is adequate and safety conditions have been met. The EP also urged the Commission to present proposals for ways to ensure that public streets in cities be maintained in a way that is both environmentally friendly and safe.

Overview of the areas of activity in relation to individual modes of transport

Roads

Roads are the primary mode of transport and will probably remain so in the future. In addition to the problem of overloading the roads, already

addressed above, the issue of payment for the use of roads has been a central concern in Europe for some time. The legislative package of 8 July 2008 on greening transportation included included provisions for steering the transportation sector towards sustainability.[19] The prime concern of the Commission was that the prices in the transport sector reflect the true costs to society. In this way, it was intended that environmental damage and congestion would lessen over time. Beyond this, the Commission also offered proposals for efficient and ecologically sensible user fees for heavy commercial vehicles and a notification that it intended to call for a 50% reduction in the noise levels of rail freight traffic. At the time, the proposal to amend the directive on raising the tariffs on heavy commercial vehicles using certain streets was at the heart of this strategy.[20] On 12 September 2011 the General Affairs Council adopted the amendments to the Eurovignette Directive.[21] The previous Eurovignette Directive of 17 June 1999 only allowed Member States to raise user tariffs on time-dependent fees for road use (per day, week or year) or to charge tariffs based on distance (per kilometre driven) for transport trucks larger than 3.5 tons (the user-pay principle). Now Member States are allowed to freely decide whether they wish to implement the polluter-pays principle. That is, when raising tolls on certain roads for commercial vehicles exceeding 3.5 tons, Member States can choose whether to not only apply a toll to cover the cost of using the roads, but whether to increase the toll to cover the external costs that arise due to traffic-related air or noise pollution. Member States are encouraged to set aside the revenue from the toll for projects in the transportation sector, especially projects that will enhance the transport network.

Measures like this do not mean that the issue is off the agenda. The Commission's long-term goal is to replace the patchwork of different road and congestion charges in Europe and introduce a measure of uniformity. According to the informal working paper of the Commission on the transport White Paper, by 2020 a binding, harmonised internalisation regime for commercial vehicles should be introduced across the entire highway network. The longer-term goal is to increase user charges so that they reflect the cost of wear and tear, as well as the cost of congestion, air pollution and noise.

In 2016, at the end of the first phase, traffic-related taxes and charges are to be restructured. This restructuring will include an examination of fuel taxes, involving clear labelling of the energy and CO_2 components, as well as the introduction of an obligatory infrastructure tax on transport trucks. Moreover, the Commission intends to assess all of the existing regulations regarding charges on transport trucks in the EU, with a view to harmonising them with the EU treaties. The internalisation of all external costs will then be expanded step-by-step to include all modes of transport. The creation of a common framework to use traffic-related revenue for the further development of an integrated transport system is also planned. In the second phase, the Commission intends to bring about, by 2020, the complete and obligatory internalisation of external costs across the entire transport spectrum.

In order to make it possible to have sustainable traffic on secure streets, with fair competition and good working conditions, the Commission is working on harmonised, transparent and unified social, security and competitive conditions. Its goal in the years leading up to 2020 is to support and deepen the dialogue between the social partners. The Commission will also rework the regulations concerning tachographs so that these become cheaper to operate, and will allow police and other law enforcement officers access to the EU register of transportation companies.

The goal outlined in the Commission's transport White Paper, to reduce the number of deaths in traffic accidents, is an issue that the Commission has pursued for decades (the first action programme of the Commission on traffic safety was implemented in 1993). In the Commission's second White Paper in 2001, the aim was to reduce the number of traffic fatalities by half by 2010, through the use of stronger traffic controls, the introduction of new technologies to make traffic safer and improvements in infrastructure, as well as through measures to improve driver behaviour. The strategy was successful. There were 40% fewer traffic fatalities in 2010 than in 2001. In July 2010 the Commission presented its guidelines for traffic security by 2020.[22] Among other measures, the Commission recommends the use of electronic systems that will help to improve safety and to avert danger on the

roads of Europe. The Commission believes that the introduction of 'eCall' across Europe could significantly reduce the number of traffic fatalities. In vehicles equipped with eCall, in an accident situation the rescue coordination centre responsible for the area is notified automatically. The sensor that is responsible for opening the airbag also sends an emergency signal. The location of the crashed vehicle is identified via satellite along with additional data about the vehicle, which is relayed to the rescue coordination centre nearest to the accident via the mobile phone network.

However, traffic is affected by many different factors that also play a significant role in traffic safety, for example, by an increase in the number of elderly persons or persons with disabilities who are active on the roads. The Commission determined that, in 2008, 20% of all traffic accidents leading to a death involved elderly persons (40% of whom were pedestrians). Bicycle and motorcycle riders are the next group of road users most at risk. The appropriate response here is not only to improve driving techniques but also to continue to improve the infrastructure.

Other measures to increase safety on the roads include regulating the hours per day that truck drivers can be on the road versus the time they must spend resting. The Commission proposed a regulation in July 2011, as announced in the White Paper, to amend the current regulation on recording equipment (digital tachographs).[23]

Giga-liners or mega-trucks are an issue that will have a significant impact on the coming debate concerning the further expansion of the transport of goods on the road network. The EU Commissioner for Transport, Siim Kallas, testified in March 2012 before the EP Transport Committee that he was rethinking his views on the cross-border use of mega-trucks.[24] Council Directive 96/53/EC, which regulates the length and weight of transport trucks, prohibits cross-border trips by transport trucks that exceed the regulated length and weight.[25] Commissioner Kallas is considering allowing transport trucks of up to 60 tons in weight to cross borders between Member States with bilateral agreements.

Rail

In rail transport too, the Commission's aim is to create a single common European rail area. The complete opening up of the market has so far proved to be difficult and is still not final. What needs to be done in the first place is to remove the barriers that prevent entry into national rail transport markets: these are mainly technical, but they can also be administrative and legal.

The Commission believes that in order to create a single common European rail area the market opening-up process must be completed. This would include a strengthening of the role of the European Railway Agency, as well as a clearer distinction between those who manage the infrastructure and those who provide the services. It is true that the market for rail freight has since been opened up to competition in accordance with Council Directive 2004/51/EC[26] on the development of the railway providers of the EU, as has the market for passenger transport providers since 1 January 2011 because of Directive 2007/58/EC.[27] At the same time, however, the transport of people within the Member States largely remains closed to competition.

To bring about effective market liberalisation, national security agencies and regulatory authorities have been created at the Member State level. Their task is to make it possible for companies to encounter fair and discrimination-free entry into the rail network and into the market for services offered by rail transport. They have also been given the responsibility of verifying that the principles of the fee structure and capacity regulations are properly applied. In the past there have often been difficulties in this area, especially when regulatory authorities were not properly independent of the infrastructure managers or the established railway companies. For this reason the Commission strengthened their powers in its proposal to reform the railway package.[28] In some Member States, including Germany, the structural integration of infrastructure management and railway management is still in place. In the view of the Commission, this could lead to decisions that protect the established operators from competitors and to revenue from usage charges on railway companies being misdirected.

For this reason the Commission brought charges against Germany and 12 other Member States in the European Court of Justice on 10 May 2010, claiming that Germany had failed to meet its obligations under Directive 2004/49/EC of 29 April 2004 on railway safety,[29] amending Directive 94/18/EC on the licensing of railway undertakings, as well as Directive 2001/14/EC on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure and safety certification (Railway Safety Directive). The Commission based its claim on the fact that Germany had not adopted the regulations and administrative provisions required to transpose this Directive into national law within the time stipulated, or that it had not informed the Commission thereof. The deadline for transposing the Directive was 30 April 2006. In June 2008 the Commission had already opened treaty infringement proceedings against 24 Member States, and in October 2009 it sent opinions with grounds to 21 non-compliant Member States. After evaluating the responses of the Member States, the Commission decided to sue the 13 Member States that had not yet transposed the EU directives into national law.

The Commission is of the view that rail is not especially competitive compared with other modes of transport, despite its low operating costs. Management and technical obstacles, such as the diversity of gauges, signalling systems and electrical systems, as well as missing links, bottlenecks and inefficient capacity management, mean that passenger service is promoted, while rail freight transport is regarded as too expensive and unreliable. There are still only 20 large airports and 35 large ports connected directly to the rail network. Some gains, however have been made in the meantime in the area of interoperability.

Interoperability is in fact the goal of European Parliament and Council Regulation (EU) no. 913/2010 of 22 September 2010 concerning a European rail network for competitive freight.[30] It sets down regulations for the establishment and organisation of cross-border freight transport corridors for competitive rail freight transport. In the appendix of this Regulation, the first nine freight transport corridors are identified, which the Member States involved are to put into operation between November 2013 and November 2015.

It is anticipated that the Member States will create an executive board for each freight transport corridor, consisting of representatives from the relevant authorities of the Member States. A board of directors such as this would create or become a common place (a 'one-stop shop') for increasing railway capacity and establishing priority regulations for freight and passenger trains.

On 22 July 2009, with Decision 2009/561/EC the Commission adopted a European plan for the legally binding introduction of the European Rail Traffic Management System (ERTMS).[31] The Decision provides for the equipping of certain corridors with the ERTMS by 2015, namely corridor A, Rotterdam–Genoa. Other corridors are to be fully equipped by 2020. The ERTMS is intended to replace more than 20 different national train control and command systems in Europe, which are the most significant barrier to international rail traffic. At the moment approximately 2,000 kilometres of European railway tracks have been equipped with the ERTMS.

Inland waterway transport

Inland waterway transport has now been completely privatised. It must be remembered, however, that the Rhine and the Danube also flow through third states, so the matter of privatisation needs to be nuanced. In 2006 the Commission presented a comprehensive action plan to promote inland waterway transport (NAIADES). This mode of transport is not particularly significant in and of itself, but it is an important connecting link in the trans-European traffic network, that is, in the system of 'co-modality'. In an unofficial working paper for the White Paper, the Commission explicitly addresses the desirability of moving some container transportation to the inland waterways (the use of the multimodal transportation of goods), thereby strengthening their market position. As with the other modes of transport, in order to meet environmental goals the fuels used on the inland waterways should be improved or replaced with alternative fuels. The introduction of new technologies, including compatible satellite-based information systems,

as well as the further development of the sea traffic surveillance network, SafeSeaNet, are also on the Commission's agenda, in order to ensure compatibility with the River Information System.

Air traffic

European air traffic is one of the most efficient components of the European economy. Global competition is increasing rapidly, however, and measures are needed to increase the capacity and quality of this market if it is to remain internationally competitive.

It is the Commission's view that recent events, such as the crisis caused by the volcano ash cloud, have shown how urgent it is that the Single European Sky should be completed. The foundation for it was laid with the acceptance of the first legislative package in 2004.[32] The creation of the Single European Sky made it possible to reach the goal of tripling capacity, cutting air traffic management costs in half, increasing air traffic safety and reducing the environmentally harmful consequences of flying by 10% per flight. The decisive prerequisite for achieving these goals was the rapid implementation of the new air traffic management technology, SESAR. To create the Single European Sky, a grid manager is to be introduced, with responsibility for managing scarce resources. Work continues on dividing airspace into functional blocks in order to optimise air traffic control independently of national borders.

In the 2011 transport White Paper, the Commission made it clear that airports play a key role in the creation of a single European transport area.[33] In the face of competition from the growth-oriented 'emerging markets', above all the Asia Pacific area, current airport capacity in the EU must be used more efficiently in the future. The prognosis is that, despite the global economic crisis and the anticipated 40% increase in airport capacity in the EU between 2007 and 2030, in the long run it will not be possible to meet approximately 10% of the demand for flights (around two million flights). Five large airports in Europe are already operating close to capacity (Düsseldorf, Frankfurt, London Gatwick, London Heathrow and Milan Linate); in 2030 this number will reach

19 and will include airports such as Paris Charles de Gaulle, Warsaw, Athens, Vienna and Barcelona. According to the prognosis, the resulting congestion will affect up to 50% of all passenger and cargo flights.

In order to increase the competitiveness of European airports, the Commission regards it as essential that the current European regulatory framework be reformed. Therefore, on 1 December 2011 it released an 'airport package'.[34] This includes the following documents:

- the Communication *Airport Policy in the European Union: Addressing Capacity and Quality to Promote Growth, Connectivity and Sustainable Mobility*;[35]
- a proposed regulation regarding ground handling services at EU airports and repealing Directive 96/67/EC;[36]
- a proposed regulation for common rules on the allocation of slots at European airports;[37] and
- a proposed regulation on the establishment of rules and procedures with regard to the introduction of noise-related operating restrictions at EU airports within a balanced approach and repealing Directive 2002/30/EC (the operating restrictions Directive).[38]

In the eyes of the Commission, the two biggest challenges in the future will be the optimal use of limited airport capacity and increasing the quality of services. The Commission therefore intends to adopt a 'gate-to-gate' approach, that is, to analyse operating performance of the entire air traffic network for possible optimisation. This includes the airport's connection to the transport system, the improvement of ground services, the optimal utilisation of airport capacity, the development and introduction of new technologies (such as air traffic management systems within the framework of the SESAR programme), enhanced airport coordination through the Airport Collaborative Decision-Making System (A-CDM), new opportunities for financing, improved noise protection, and transparent airport and security

fees, as well as an examination of the safety system based on a risk-assessment approach.

Maritime traffic

Approximately 40% of intra-European and 80% of international freight traffic goes by sea. More than 400 million passengers pass through European ports annually. According to the European Community Shipowners' Associations, Europe (i.e. the EU and EEA) has the largest fleet of ships worldwide. The seaports in Europe, among them Rotterdam and Antwerp, are therefore of decisive importance for the EU's economic development, as are the relevant lake and inland waterways. As the Commission describes in its White Paper, fair global competition and trade rules for maritime transport are fundamental challenges that must be met by an EU sea traffic policy (for the international aspect see the section on External relations). Another significant challenge is the environmental standards for maritime traffic. The EU's maritime safety policy can also be added to this list. Regarding the last issue alone the EU has approved three large packages of legislative proposals since 1999 (the 'Erika packages', maritime traffic safety packages following the sinking of the oil tanker 'Erika' in 1999). In the future, the work of the Commission will be guided by the 2011 White Paper as well as the Communication of the Commission of January 2009 on the relevant strategic goals for the EU's Maritime Transport System until 2018.[39] The Communication addresses the challenges discussed above, but also deals with educating experts in the context of global markets, and with job-related qualifications and improvements in working conditions (e.g. through the effective implementation of the International Labour Organisation (ILO) Maritime Labour Convention of 2006). Another goal is to ensure the high quality of maritime traffic by bringing about the 'long-term objective of "zero-waste, zero-emission" maritime transport'.[40]

In the Commission's 2011 White Paper,[41] maritime transport as the key element of inter-modality (see also the section on Trans-European Network Traffic) is discussed several times (in connection with the goal that 50% of

passenger and freight transport over distances of greater than 300 kilometres will be by rail or ship). Seaports (as the primary logistics centres) require relevant connections to the hinterland. It is important, therefore, that the ports belonging to the core network be connected to the freight rail network and, if possible, to inland waterways. It is also important to develop the capacity of short-haul maritime traffic by establishing a European maritime traffic area without borders, as is the case for air traffic. According to the Commission White Paper, a 'blue belt' around Europe will cut red tape for ships and ferries operating between EU ports. As with other modes of transport, modern traffic management and information systems need to be developed for maritime transport as well.

Within the context of the development of a transport system that conserves resources, a key agenda item for maritime transport, in addition to a reduction in CO_2 emissions from bunker oil, is a reduction in the sulphur content of marine fuel (with the Commission's proposal for a directive to amend Directive 1999/32/EC on the sulphur content of marine fuel).[42] This issue is being dealt with by the DG Environment and the Environment Council. The Commission is also considering, in the context of safety and the environment, the recycling of ships. On 23 March 2012 it put forward two proposals in this regard.[43]

On 23 March 2012, in the context of the 2011 White Paper, as well as the 'Social Agenda for Maritime Transport' described in the 2009 Communication, the Commission released three proposals for directives: *Proposal for a Directive Amending Directive 2009/16/EC on Port State Control,*[44] *Proposal for a Directive concerning Flag State Responsibilities*[45] and *Proposal for a Directive on the Maritime Labour Convention.*[46]

One issue that the Commission will certainly take up again very soon is the opening up of port services to competition. In a Commission press release on 8 November 2011, Commissioner Kallas gave notice that he would put forward a bundle of proposals in 2013 intended to help ports preserve their competitiveness so that the significant prospects for growth in the port sector could be realized.[47] The Commission presented a proposal

on this issue for the first time in 2001, with its package of measures for the development of clearer regulations and an open, transparent process for access to port services.[48] However, in 2003 the EP rejected this proposal, as it did a renewed proposal in 2006.[49] In a Communication on European ports policy,[50] the Commission once again took up the issue of framework conditions for competition within and among ports. The usual conflict between competitiveness and job security and the danger of wage dumping will no doubt arise again.

The Commission has also given notice that it intends to actively pursue the issue of safety requirements for cruise ships.

Galileo and other new technologies

New information and communication technologies play an important role in the area of European transport policy. The development of technologies that improve safety and security can play a decisive role in reducing the number of traffic fatalities. Above all they support the introduction of intelligent mobility systems and lead to the better use of capacity and to an increase in profitability.

In addition to the introduction of a management system for land and maritime traffic, the Commission 2011 White Paper explicitly names among its goals the introduction of the satellite navigation system Galileo, which is also part of the EU's space strategy.[51]

In connection with the gradual opening up of the transport market in the 1990s, the ERTMS, the trans-European high-speed rail network (TEN-R) and the Galileo satellite navigation system were developed through major European research and development projects. In addition, SESAR was launched as a programme to improve the infrastructure of airport management.[52]

The global satellite navigation programme, Galileo, is—alongside the existing EGNOS (the European Geostationary Navigation Overlay Service), intended to improve the accuracy and reliability of GPS signals in Europe—the EU's central technology project. Both represent, and not just in the area of traffic, a fundamental contribution to maintaining and enhancing the competitiveness of Europe's economic and technological standard. Galileo should go into service by 2014/15 with an initial constellation of 18 satellites. Expansion to the full constellation of 30 satellites is planned for completion by the end of the decade. After the launch of the first two operational Galileo satellites on 21 October 2011, additional satellites were launched into space on 19 and 20 October 2012. From 2013 the launches are to take place at shorter intervals. Since 1 Sep 2012, the European GNSS Agency (GSA), which will be responsible for the operation of Galileo and EGNOS from 2014/15, has been located at its new headquarters in Prague.

Integrated traffic control systems and information systems are a vital part of a modern traffic system. They can be used to direct freight flows and for booking and payment systems. In the current (seventh) EU Research Framework Programme (2007–13), resources have been made available for research and innovation in the field of traffic. These resources are to be used for research into expanding the capacity of the rail networks and maritime transport, improving urban mobility, promoting green car initiatives, creating infrastructure for electro-mobility and introducing more intelligent traffic systems. DG Move is currently developing a strategy paper for future research activities and innovation in the mobility sector.

Trans-European Network Traffic

Together with the telecommunications and energy infrastructure, the traffic infrastructure is anchored in the Lisbon Treaty as the Trans-European Network Traffic (TEN-T).[53] The goal of TEN-T is to strengthen the internal market and to contribute to the economic, social and territorial integrity of the EU. In the 2011 transport White Paper (see above) the Commission

has included more goals directly or indirectly relevant to the trans-European traffic network (realising a TEN-T core network, connecting airports to the railway network, completing the European high-speed railway network, and also creating a European multimodal traffic information system).

Harmonising and connecting traffic infrastructure within the EU, as well as expanding it, have for some time been key elements of EU policy and they have considerable economic consequences, making the free movement of persons and goods and consolidating social and economic cohesion possible. One goal of this policy has been to bind the insular and inward-looking regions on the edges of the EU to the central regions and to better connect the territory of the EU with bordering third states. In June 1990, the then European Transport Council produced the first action plan for a trans-European network for traffic, energy and telecommunications. In the 1990s the first cross-border initiatives followed to establish high-speed railways (e.g. the creation of a high-speed rail line between Paris and Budapest/Bratislava, the 'Magistrale for Europe'). In the Maastricht Treaty, which came into effect on 1 November 1993, the concept of a trans-European network was given legal footing for the first time. This was followed, at least legally, by another divergence from the national point of view in the area of transport, and one which had held sway for a long time. In December 1994 the European Council presented a list of 14 major key traffic projects, including a project to create stretches of cross-border high-speed rail lines and another to expand airports. To facilitate their implementation, European financing instruments, supported by the European Investment Bank, were created, which included contributions from national budgets. Two years later, in 1996, the EP and Council adopted the first guidelines for the construction of a trans-European traffic network,[54] which brought the structures responsible for the various transit modes into a unified framework and established criteria for selecting and financing projects of common interest (with a clause requiring the Commission to review and revise this every five years). In 2001 the 1996 guidelines concerning port structures were expanded,[55] and in 2004 the guidelines were revised again[56] to

create a list of 30 preferred large-scale traffic projects, including the 14 projects named in the 1994 guidelines.

The TEN-T as a multimodal traffic network and its further expansion must, therefore, include all modes of transport. As the Commission states in its 2011 White Paper, the transportation industry as a whole is facing structural changes. From the various elements mentioned above, it is clear even today that mobility in Europe will become more expensive. The Commission has therefore urged that there be more competition and more participation from the private sector. This also applies to the expansion of the TEN-T.

On 19 October 2011 the Commission presented its *Proposal for a Regulation on Union Guidelines for the Development of the Trans-European Transport Network* (TEN-T)[57] and a *Proposal for a Regulation Establishing the Connecting Europe Facility.*[58] In light of the new challenges for European transportation policies outlined in the White Paper, the Commission presented its ideas in the form of a concrete long-term strategy for the TEN-T, operational until 2030/2050. The White Paper was preceded by the release on 4 February 2009 of a Green Paper, *Towards a Better Integrated Trans-European Transport Network at the Service of the Common Transport Policy*, and a consultation phase until the end of April 2009. The implementation of the TEN-T policy was not satisfactory, and there was a continued preference for national projects, so the Commission decided to initiate a reform process and presented various strategic options for the future for discussion. On 4 May 2010 a working paper was presented, in which the Commission stated that a large majority of European stakeholders favoured the further development of the TEN-T with a two-tier structure: a comprehensive network and an intermodal core network.[59]

The Commission believes that an efficient traffic system is a necessary foundation for the economy, since regions that are difficult to reach cannot develop. By 2050 goods transport in Europe will probably increase by 80% and passenger transport by more than 50%. However, CO_2 emissions are to be reduced by 60% by 2050.[60]

In order to meet these challenges, the Commission believes that a fundamentally new infrastructure policy is necessary. The present European transport network is like a patchwork quilt. Uneven levels of infrastructure mean unequal accessibility and unequal access to markets. EU Member States are inadequately connected both to each other and to neighbouring countries. Missing links, bottlenecks and inefficient capacity management handicap traffic flows. Technical barriers remain, such as differences in track gauges, electrical systems and signal technology in the context of railway traffic, and in traffic management as a whole. Different modes of transport are poorly connected to each other. For example, only 20 large airports and 35 large ports have a direct connection to the rail network. Moreover, there is virtually no information technology connection between the various modes of transport. Furthermore, the Commission regrets that there is very little innovation, especially in the area of CO_2 reduction.

The Commission has proposed, therefore, that the present patchwork of priority projects be replaced by a 'core network'. This core network will be the backbone of a sustainable transport system and should be built by 31 December 2030. It should ensure a broad level of regional accessibility and establish common minimum standards. All modes of transport (road, rail, air, inland waterway and maritime), as well as intermodal platforms, will be integrated into the core network. It will connect the large social and economic centres and have connections to third countries (ports, airports and land connections). Eighty-three of the most important European ports are to be connected to the rail and road networks, and 37 major airports are to be connected to the rail network. The core network will include 15,000 kilometres of track built for high-speed rail traffic and will create 35 large cross-border projects whose completion will relieve bottlenecks. Ten core network corridors will contribute to the efficient operation of the core network. Each has at least three modes of transport, in three Member States, and two cross-border connections. The technical requirements of the core networks should guarantee interoperability across the entire network. The ERTMS should be introduced on a broad scale across Europe to control rail traffic. Norms for road safety (e.g. for tunnels) will

also be harmonised, as well as the requirements of the recharging infrastructure for electric vehicles.

The new TEN-T core network will be complemented and supported by the comprehensive network provided at the regional and national levels. The Commission's goal is that by 31 December 2050 the vast majority of European citizens will not be more than 30 minutes from this comprehensive network. In all, the new traffic network should be more secure and less susceptible to congestion, and allow for rapid travel without friction.

The Commission estimates that €500 billion will be required to finance the core network by 2030. By 2020, €250 billion will be required. Member States and other public and private bodies will drive the project as primary investors. On 29 June 2011 the Commission presented a proposal to create the Connecting Europe Facility (CEF) in the context of a multi-annual financial framework. The CEF will have a budget of €50 billion, of which €31.7 billion will be spent on modernising the trans-European transport network (€10 billion will come from cohesion funds). The funds should provide the seed money and stimulate more investment from Member States to create cross-border connections and fill gaps in the transport network. Of the funds, 80%–85% is to be spent in three-year periods on horizontal priorities (e.g. financing SESAR and the ERTMS), and to develop the ten core network corridors and other important sections of 10 core network. On a yearly basis, 15%–20% will go to ad hoc projects that are either part of the core network or the comprehensive network.

Efforts to mobilise private capital in the framework of public–private partnerships, which the Commission has promoted for some time, have not yet had the desired success. Financing projects remains one of the most significant challenges. But without Europe-wide agreement on priority projects, and without combining national resources, the goal of a European transport network will not be achieved.

The Commission's proposed Regulation is currently going through the legislative process. The Council of Transport Ministers reached a general

consensus on 22 March 2012. The Member States agreed, in view of the significant financing needs and the planning competence of the Member States, to institute a general planning and budget moratorium. This decision particularly weakened the legally binding time frame in the Commission proposal to create the core network by 2030 and the comprehensive network by 2050. In view of the ongoing debate in the EP it should not be assumed that the Commission's proposal will be adopted unaltered.

The EU and its neighbours

The Treaty of Lisbon obliges Europe to build special relationships with its neighbourhood.[61] The EU should work together with third countries to promote projects of common interest and to ensure the interoperability of networks;[62] it also has its own foreign relations competencies.[63]

Following the 2004 enlargement round, in which 10 new Member States acceded to the EU, the EU's transport planning with its neighbours had to be adapted to the new geographic challenges. Naturally, this was also true for all of the subsequent enlargement rounds, such as the accession of Bulgaria and Romania in 2007. Moving the external borders east and south meant that the plans then in place for the TEN-T and traffic flows within the EU had to be realigned or revised (see above).

The Commission intends to vigorously develop transport policy with the neighbourhood (which includes the new accession states) in order to meet the challenges of traffic flows. These challenges touch on market integration as well as infrastructure. The first steps will be to remove barriers to cross-border traffic and to ensure that neighbouring countries have a transport system with high standards of safety, security, social security and environmental protection.

In the transport White Paper, the relationship with the EU's neighbours is dealt with in the section 'The External Dimension'.[64] Shortly after the White

Paper appeared, the Commission proposed a new action plan for cooperation in the area of transport with its neighbours,[65] and thereby made clear its previously announced intention to develop the European transport and infrastructure policies with regard to the immediate neighbours of the EU and to open up new markets for transport service providers. With this plan, the Commission is pursuing the goal of expanding transport connections with the EU's eastern neighbourhood (Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine), with its southern neighbours (Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, the occupied Palestinian territories, Syria and Tunisia), with the accession candidates (the Former Yugoslav Republic of Macedonia, Montenegro and Turkey) and with potential candidate countries (Albania, Bosnia and Herzegovina, Serbia, and Kosovo), and of strengthening market integration depending on the conditions specific to each candidate country. Greater integration of the transport market between the EU and its neighbourhood will make transport connections quicker, cheaper and more efficient. The plan identifies short-term and long-term measures for road, rail and air traffic, as well as improvements to infrastructure connections.

It is road transport above all that plays a key role in the trade flows between the EU and its neighbours. The Commission still sees the waiting times at the border caused by administrative procedures as the primary barrier to the efficient movement of goods between the EU and its neighbours to the east. These delays are responsible for 40% of the total transport time. The Commission also wants to adopt initiatives with respect to the low standards of road safety in neighbouring countries.

In the last 10 years there has been, according to the Commission, an increase of 7% in the amount of rail freight traffic between the EU and its neighbouring countries to the east (Belarus, Moldova and Ukraine). This is expected to grow by 40% by 2020. The Commission is of the view that closer cooperation with neighbouring countries could provide more positive incentives to open up the European rail transport area.

Greater integration of air traffic with neighbouring countries should lead to the creation of a larger uniform European air space, which would then

include approximately one billion people. Between 2004 and 2009, the number of passengers travelling between the EU and its neighbours to the south grew at an average annual rate of 6.7%; between the EU and its neighbours to the east it grew by no less than 11.6%.

In the area of maritime transport, cooperation with the partner countries of the Mediterranean zone is especially important in order to strengthen safety, security and maritime surveillance.

In the area of infrastructure connections, the Commission first intends to concentrate on the definition of strategic networks on a regional level in the European neighbourhood. These should serve to extend the TEN-T. As a further step, priority projects will be identified that are in the interests of both parties and which will especially improve the interoperability of transport systems in the EU and its neighbourhood.

Another important approach to cooperation, especially to expanding the transport infrastructure (roads, rail and water), could be the relatively new concept of the macro-region, for example, the Baltic Sea macro-region, which is part of the EU Strategy for the Baltic Sea Region, adopted by the European Council in October 2010. It encompasses the regions of the countries bordering the Baltic Sea, but also the Danube macro-region, which was adopted by the European Council in June 2011.[66] There are third countries within the large geographic expanses of these regions. The structure of the macro-regions is an important factor in neighbourhood policy and can also play a significant role with respect to cooperation in the area of transport.

External relations

The EU's competency with respect to agreements with third countries or international organisations and the binding character of these agreements are dealt with in Article 216 of the TFEU. According to this article, as a rule,

the EU has certain competences for external relations if it also has these competences within the EU, according to both Article 91(1)(c) of the TFEU on measures to improve traffic safety and Article 91(1)(d) of the TFEU on regulations for particular purposes.

The Commission's 2011 White Paper, with its roadmap to 2050, also includes a chapter on 'The External Dimension'.[67] In it the Commission explicitly highlights the need to extend the internal market provisions and strengthen the dialogue on traffic policy issues with the most important partners.[68] Intensive cooperation is necessary to overcome barriers to transport (e.g. implementing the interoperability of traffic management systems or the use of fuels that are not environmentally friendly), but is also necessary in the area of traffic safety.

Air and maritime traffic have been the subject of intensive international cooperation for some time, since these two modes of transport are particularly at the mercy of international competition. For this reason, international agreements are especially desirable in the future in these areas as well. Bilateral agreements between individual Member States and third countries, or even multilateral agreements, can be a first step, but are contradictory in many areas to the concept of a genuine common market. This is clear in the area of air traffic, for example. International legal frameworks are desirable when it is a case of a global challenge such as climate change and the intent is to respond in a way that is neutral to competition. On the other hand it is important that Member States speak with one voice in international organisations such as the International Civil Aviation Organization (ICAO) or the International Maritime Organization (IMO).

As the Commission notes in the White Paper, the EU, alongside international organisations, should strive to aim for the universal application and enforcement of high standards of technical safety, security, environmental protection and working conditions and to combat piracy.[69] With international partners and international dialogue—in the IMO and ICAO—competition-neutral global solutions are impossible to find. There will always be tension in such meetings between the Commission and particular

corporations (e.g. the shipowners or the airlines) if legislative proposals are introduced in the EU that might put European companies at a competitive disadvantage. This is especially true if these proposals are not in harmony with internationally adopted regulations, for example, the IMO and the International Convention for the Prevention of Pollution from Ships, or the International Convention on the Safety of Life at Sea, but rather create standards that are stricter than these or build on unilateral measures of the EU that have not been adopted by international organisations. One such current instance is the inclusion of air traffic in the emissions trading regime that came into effect in the EU on 1 January 2012.[70] If such rules are not adopted internationally, which does not appear likely, the climate goals described above will not be attained.

The global challenge of charting a course successfully in the tension between the EU's role as a trail-blazer and maintaining competitiveness, that is, not to founder under the challenge, will be decisive for the development of air and maritime traffic and the European companies active in this area.

Cooperation with international partners and in international organisations will play an even larger role in the future if the EU is to successfully meet the global challenges of the twenty-first century.

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Mobilising Justice Policies to Fully Support Growth and Stability in the EU

Introduction

The following text is an adapted version of a Resolution adopted at the European People's Party (EPP) Congress in Bucharest, Romania, 17-18 October 2012.[1]

The EPP has always promoted EU policies that will make a strong contribution to growth and job creation in a well-functioning internal market. In view of the current financial and economic crisis, we have to make sure that all EU policies are mobilised to fully support growth and stability, and that EU instruments of law, as well as national policies, can play an important role in reaching this goal.

Efficient justice systems in all EU Member States and a regulatory environment strongly anchored in the rule of law can make a significant contribution to creating an investor-friendly climate and legal certainty for businesses and consumers. At the same time, they lay key structural foundations for sustainable economic growth, which is much needed.

Actions at the EU and national level aimed at strengthening a sound and secure legal environment are, therefore, a central feature of the structural reforms currently underway in all EU Member States.

Efficient justice systems in all Member States

Economic growth, institutional efficiency and the rule of law are directly correlated. Efficient, independent courts delivering and enforcing justice swiftly and in a reliable manner are key to increasing the confidence of both businesses and citizens, and to ensuring respect for fundamental rights, including the right to a fair trial and property rights.

Dysfunctional and unclear procedures, resulting in long delays in the judicial system, seriously affect the efficient conduct of all economic activities. They add legal uncertainty and extra costs to the enforcement of laws and contracts. Moreover, late payments, and the length of time needed to obtain a resolution from the justice system, place limits on finances and increase uncertainty for businesses. In turn, long delays trigger insolvencies and boost unemployment. They also affect credit and interest rates for businesses, as well as tax collection, labour disputes, and so on. Small- and medium-sized businesses (SMEs[2])—which must be at the heart of all economic policies—are particularly vulnerable.

Actions at the national level aimed at increasing the efficiency of justice systems and reducing backlogs foster a more investment-friendly business environment. Ongoing work in countries such as Ireland, Portugal and Greece, and general reforms elsewhere across the EU show how significantly swift and efficient justice can contribute to growth—for example, by creating certainty and trust that investments are secure.

At the EU level, growth-oriented justice policies will contribute to ensuring that European economies generate more trade and jobs, whilst reducing red tape. Europe must now maximise the growth opportunities offered by its internal market. The Digital Single Market, in particular, offers growth potential for businesses and makes cross-border transactions simpler. Once achieved, a fully functioning Digital Single Market could boost the EU's gross domestic product by as much as €110 billion a year and bring welfare gains for EU consumers in the region of €204 billion.[3]

However, consumers and businesses still buy and sell closer to home. After decades of integration, 9 out of 10 EU companies still do not export. The majority of those that do (62% in business-to-business and 57% in business-to-consumer transactions) export to no more than three EU countries. It is a fact that a number of obstacles still exist to cross-border trade in the EU. Companies and consumers are held back by a lack of trust,

very often caused by actual or perceived divergences in national laws, particularly when it comes to cross-border or online transactions.

EU proposals in the field of justice will contribute decisively to completing the Digital Single Market and to providing the necessary legal certainty for businesses and citizens to engage in cross-border transactions.

Cutting red tape in civil and commercial proceedings

Easy access to justice

For the Digital Single Market to function properly, consumers and businesses need easy access to justice. Access to the courts in Europe should be predictable and transparent. To strengthen confidence in judicial systems and to ensure good cooperation between courts in the different Member States and the free circulation of judgments in the EU, it is necessary to make the cross-border recognition and enforcement of judgments in civil and commercial proceedings simpler and faster.

Small-claims procedure

Better enforcement of commercial claims can significantly help to improve the business environment. Removing unnecessary steps in enforcing judgments in cross-border disputes can cut red tape and costs. Useful steps have already been taken to meet these objectives in the form of the European procedures on small-claims and payment orders.

Further efforts are needed to make the small-claims procedure (effective since 2009 for sums under €2,000) more widely known and used. As a priority, the question of whether the small-claims procedure should also be available for claims between €2,000 and €10,000 should be explored.

Quick and simple recognition and enforcement of cross-border judgments

Within a functioning internal market, a judgment in civil and commercial matters given by a court in one EU Member State should be quickly and simply recognised and enforced in all other EU Member States. Following calls for the abolition of the outdated and costly *exequatur* procedure[4] in civil and commercial matters, the European Commission has been proposing this for a long time. On average, an *exequatur* costs a company or an individual €2,000 in a straightforward case and almost €13,000 in complex cases. An *exequatur* also involves the aggravation of going through intermediary proceedings that can take up to 12 months. It is now time to finalise the reform of the Brussels I Regulation to simplify the legal environment and to reduce the cost of cross-border transactions. This would mean that a judgment rendered in one Member State would be recognised without special procedures in another Member State.[5]

Currently European law ensures access to the courts only if the defendant is established in Europe. As soon as a defendant is established outside Europe, national law applies. The Commission has proposed removing this old-fashioned distinction regarding where parties live. It should not matter whether a defendant lives in London or in New York.

Similarly, the Commission is proposing changes to strengthen *arbitration agreements* in Europe. At present, parties can effectively obstruct such agreements by shopping around in Europe and trying to get an agreement declared invalid. This creates unnecessary litigation and leads to additional costs and delays for businesses.

As part of the reform, parallel proceedings and abusive litigation tactics will be prevented. Strengthening arbitration agreements, as well as simplifying recognition across borders of judgments in civil and commercial matters, will be major contributors to economic recovery and growth.

European Account Preservation Order

New rules on cross-border debt recovery would help European businesses retrieve the 63% of cross-border debt which currently remains unclaimed.[6] Giving creditors more certainty about recovering their debt will increase confidence in trading within the EU's single market, particularly in economically uncertain times.

Europe needs to agree quickly on the creation of a user-friendly European Account Preservation Order that protects creditors' interests effectively throughout the internal market and at the same time provides adequate protection for debtors. The use of this order would facilitate the recovery of up to €600 million in cross-border commercial debt every year.[7]

Smart insolvency proceedings

Smart insolvency proceedings could be essential to ensuring the protection and survival of some businesses and to safeguarding jobs: instead of being wound up, these businesses would have access to funds to survive. Modernising the EU Insolvency Regulation to strengthen the internal market would stimulate a modern and growth-friendly insolvency regime across Europe.

The European Commission should swiftly come up with proposals to simplify the rules for the cross-border recognition of insolvencies; to start working on proposals to align and modernise national insolvency rules on the basis of a system where creditors are adequately protected, while legitimate businesses can get a realistic 'second chance'; and to invest in the entrepreneurial spirit of Europeans.

Reforms of EU data-protection laws to stimulate the Digital Single Market

The Internet economy is bursting with innovations. We can send messages to people on another continent with the tap of a finger on a screen. We can instantly update our friends and family on the birth of a child or send them our latest holiday pictures. We can entrust our private data to a cloud service provider without knowing where and how this personal data will be stored and processed.

All these technological developments are welcome drivers of innovation, growth and job creation. But is our Digital Single Market equipped for data that know no geographic boundaries? How can we enable the free flow of information while making sure that people's personal data are well protected?

Modern European data-protection rules could strongly stimulate the development of the digital economy across the EU's single market. Simplifying the legal environment by means of a single set of rules would reduce administrative burdens for businesses and remove barriers to market entry, in particular for micro-, small- and medium-sized enterprises. Instead of having to grapple with a patchwork of different and often contradictory rules from the 27 Member States, European businesses wanting to operate across borders would be served by a modernised and uniform data-protection legislation that would remove barriers to market entry and lead to savings of about €2.3 billion per year in administrative requirements.

The new data-protection rules will unleash the potential of the Digital Single Market. The directly applicable Brussels I Regulation (one single law) and the 'one-stop shop' for companies will greatly simplify the regulatory environment within the internal market, provide more clarity and reduce the administrative burden for all businesses. For businesses operating in several Member States, this will be a giant leap forward. Multinational business will find a more consistent, uniform and simplified regulatory environment.

This is not a reform for big business alone. SMEs will also benefit from simpler and more consistent rules. Small companies will find it easier to expand across borders.

At the same time, a strengthened set of rights for the individual can address consumers' concerns about the protection of personal data when shopping online and help boost confidence about purchasing products in the digital environment. Today 70% of European citizens are worried about the way companies handle their personal data. By increasing consumer confidence in the online environment, we will stimulate online shopping and give a further boost to the Digital Single Market.

A common sales law to stimulate cross-border trade online

As businesses try to recover from the economic crisis, specific EU actions should aim to make cross-border sales and purchases in the single market easier and cheaper, namely, by eliminating trade barriers. At the moment different contract law rules at the national level exist alongside different mandatory national rules in the field of consumer protection. Traders who want to make use of the internal market have to adapt their contracts to the different national laws of the 27 Member States, which prevents them from benefiting from economies of scale. Only 6% of online purchases lead to transactions across borders in the EU today; traders often do not deliver their products to other Member States because of different contractual rules.

Against this background, the European Commission has finally proposed an optional instrument in the form of the Regulation on a Common European Sales Law. An optional instrument has the advantage of reconciling three important policy objectives:[8]

- the single market objective, as an optional instrument would allow traders to deliver products to all Member States on the basis of one contract law regime;

- freedom of contract, as the application of the rules of an optional instrument always depends on the choice of traders and consumers; and

- the principle of subsidiarity, as an optional instrument does not interfere with the different legal traditions of the Member States but leaves national civil codes and contract law legislation untouched.

Europe is on a quest for new growth opportunities, and the European Commission proposal is therefore particularly timely. It has been demonstrated that bilateral trade between countries which have a legal system based on a common origin (such as common law or the Nordic legal tradition) is 40% higher than trade between two countries without this commonality. An optional common European contract law regime could be expected to have similar effects on trade and growth across Europe. Today only 7% of European consumers buy online from another Member State and only 9.3% of businesses sell across EU borders.[9] Businesses wishing to carry out cross-border transactions may have to adapt to up to 27 different national contract laws, translate them and hire lawyers at an additional cost of €10,000 on average for each additional export market. European traders forego €26 billion in cross-border transactions each year because they are dissuaded by contract law barriers.

The focus of further work should be on ensuring that the optional rules are user-friendly and drafted in a simple and clear way that stimulates easy adoption by practitioners.

For the first time, the European Commission has not proposed replacing existing national law with EU law but instead has proposed making an additional harmonised instrument available for traders to choose—a turning point in European law-making. This instrument provides a welcome opportunity in terms of developing the field of justice in the European area, which has a vital contribution to make to the free movement of goods. Moreover, the proposed instrument will also benefit the functioning of the internal market and growth in the digital economy, while the different legal

systems, traditions of the Member States and the principle of subsidiarity will remain intact. Therefore, EU justice ministers and the European Parliament need to work actively on this first optional instrument.

It would also be of great benefit if the European Council were, by July 2013, to discuss the practical experiences of this first optional instrument. A more general discussion on the added value of optional instruments in EU law-making in further specified areas where there is a clear growth potential, such as the field of insurance contract law, should also be looked at.

Combating unlawful conduct of business

Businesses operate in an environment where numerous rules ensure their balanced operation. Infringement of these rules should be appropriately penalised in order to ensure a safe and secure climate for investment and entrepreneurship. However, businesses should not be subject to the permanent threat of numerous and unclear provisions, which could result in an unwillingness to undertake economic activity. At the same time, the need to recognise cross-border bans on economic activity, where decided by courts, should be considered. Otherwise, the operation of the internal market will be undermined by rogue businesses.

Women on company boards

Currently women are at a clear disadvantage: only 13.7% of the board members of Europe's largest publicly listed companies are female. At the same time, women account for 60% of new university graduates. Getting more women into the higher segments of the labour market is one way to improve Europe's competitiveness. It will also help to achieve the Europe 2020 goal of raising the employment rate for adults to 75%.[10] For the benefit of our economy, we simply have to make better use of the talent pool of highly skilled women.

The Commission, therefore, has proposed legislation with the aim of attaining an objective of 40% of the under-represented sex in non-executive board-member positions in publicly listed companies, with the exception of SMEs. Boards are currently dominated by one gender: 85% of non-executive board members and 91.1% of executive board members are men, while women account for 15% and 8.9%, respectively.[11]

The proposed directive sets the objective that 40% of the non-executive directors of listed companies should be women. Companies that have a lower share of women among non-executive directors will be required to make appointments to those positions on the basis of a cooperative analysis of each candidate's qualifications, applying clear, gender-neutral and unambiguous criteria. Given equal qualification, priority must be given to female candidates. The objective of attaining at least 40% membership of women for the non-executive positions should thus be met by 2020, while public undertakings—over which public authorities exercise a dominant influence—will only have until 2018. The proposal is expected to apply to around 5,000 listed companies in the European Union. It does not apply to SMEs or to non-listed companies.[12]

Consular protection

Sometimes EU citizens find themselves in a country in which their native country has no embassy or consulate. These people have the right to turn to the diplomatic representation of any other EU Member State for protection. This EU Member State has to assist them as though they were its own nationals.[13] More than five million Europeans travel to countries where their home Member State has no embassy or consulate. Another 1.7 million live in such countries. The proposed EU directive provides for clearer and simpler cooperation between Member States' consular authorities.[14]

Protecting European taxpayers' money

The EU budget should continue to be reoriented towards investments in growth-enhancing initiatives. To ensure that the value of each euro from the EU budget is maximised, Member States should fight fraud with equal determination. This requires that fraud against the EU budget is punished in all Member States with equally deterrent criminal sanctions. Better coordination among national authorities and EU bodies, including the European Anti-fraud Office and Eurojust, should make the common fight against crimes affecting the financial interests of the EU more effective. Moreover, the establishment of a European Public Prosecutor's Office, in line with the ambitions of the Treaty of Lisbon—Article 86 of the Treaty on the Functioning of the European Union—would ensure that these crimes are effectively prosecuted across the continent.

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Notes

[1] European People's Party, 'Resolution on Justice for Growth: Mobilising Justice Policies to Fully Support Growth and Stability in the EU of 17-18 October 2012, European People's Party Congress in Bucharest', accessed at http://www.epp.eu/documents-library?field_doc_section_tid=All&page=1 on 7 February 2013.

[2] An SME is a company with fewer than 250 employees and an annual worldwide turnover not exceeding €50 million.

[3] European Parliament, Committee on the Internal Market and Consumer Protection, 'On Completing the Digital Single Market', Report, 2012/2030(INI) (26 October 2012), 25.

[4] An *exequatur* is an authorisation, made by a court within a specific country, of the enforcement within that country of a judgment given abroad.

[5] Council Regulation (EC) no. 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, OJ L12 (16 January 2001), 1, Art. 33.

[6] European Commission, 'Civil Justice', accessed at http://ec.europa.eu/justice/civil/index_en.htm on 7 February 2013.

[7] European Commission, *Proposal for a Regulation of the European Parliament and of the Council Creating a European Account Preservation Order to Facilitate Cross-border Debt Recovery in Civil and Commercial Matters*, COM(2011) 445 final (25 July 2011).

[8] European Commission, *Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law*, COM(2011) 635 final (11 October 2011).

[9] European Commission, Justice, 'Common European Sales Law to Boost Trade and Expand Consumer Choice', Press Release (11 October 2011), accessed at http://ec.europa.eu/justice/newsroom/news/20111011_en.htm on 7 February 2013.

[10] European Commission, 'Europe 2020 Targets', accessed at http://ec.europa.eu/europe2020/targets/eu-targets/index_en.htm on 7 February 2013.

[11] European Commission, 'Women on Boards: Commission Proposes 40% Objective', Press Release (14 November 2012), accessed at http://europa.eu/rapid/press-release_IP-12-1205_en.htm on 7 February 2013.

[12] Ibid.

[13] European Commission, *Proposal for a Council Directive on Consular Protection for Citizens of the Union Abroad*, COM(2011) 881 final (14 December 2011), 2.

[14] European Commission, *Proposal for a Council Directive on Consular Protection for Citizens of the Union Abroad*, 4

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Research, Innovation and Technology Development Policy

Introduction

At a time of public budget constraints, major demographic changes and increasing global competition, Europe's competitiveness, our capacity to create millions of new jobs to replace those lost in the economic crisis and, overall, our future standard of living, depend on the EU's ability to drive innovation in products, services, business and social processes. This is the reason that innovation has been placed at the heart of the Europe 2020 strategy for smart, sustainable and inclusive growth.[1]

Europe 2020 puts forward three mutually reinforcing priorities:

- smart growth: developing an economy based on knowledge and innovation,
- sustainable growth: promoting a more resource-efficient, greener and more competitive economy, and
- inclusive growth: fostering a high-employment economy to deliver social and territorial cohesion.

Progress on each of these priorities requires increased effort in research and innovation.

Smart growth means strengthening knowledge and innovation as drivers of our future growth. This requires improving the quality of our education, strengthening our research performance, promoting innovation and knowledge transfer throughout the Union, making full use of information and communication technologies, and ensuring that innovative ideas can be turned into new products and services that create growth, quality jobs and help to address European and global societal challenges. But, to succeed, this must be combined with entrepreneurship, finance, and a focus on user needs and market opportunities.

Under the heading of smart growth, the European Commission has proposed the Innovation Union flagship initiative among a set of six other major EU policy priorities. The flagship initiatives will commit both the EU and the Member States. EU-level instruments will be fully mobilised to tackle bottlenecks and deliver the Europe 2020 goals. The aim of the Innovation Union is to refocus research and development (R&D) and innovation policy on the challenges facing our society, such as climate change, energy and resource efficiency, health, and demographic change. Every link should be strengthened in the innovation chain, from 'blue sky' research to commercialisation.

The EU has world-leading researchers, entrepreneurs and companies, and unique strengths in our values, traditions, creativity and diversity. The EU has made great strides in creating the largest domestic market in the world. European enterprises and civil society are actively engaged in emerging and developing economies around the world. Many world-changing innovations can be traced to Europe. But the EU aims to do better in the world's rapidly changing global economy.

The EU suffers from the following difficulties:[2]

- Underinvestment in our knowledge foundation: other countries, like the US and Japan, are out-investing us, and China is rapidly catching up.

- Unsatisfactory framework conditions, ranging from poor access finance and the high costs of Intellectual Property Rights (IPR), to slow standardisation and the ineffective use of public procurement: this is a serious disadvantage when companies can choose to invest and conduct research in many other parts of the world.

- Too much fragmentation and costly duplication: we must use our resources more efficiently and achieve critical mass.

The Innovation Union flagship initiative launched on 6 October 2010 is intended to set out a bold, integrated and strategic approach, exploiting and leveraging EU strengths in new and productive ways, thereby maintaining the

economic foundation that supports our quality of life and our social model as our population ages. The present article describes the Innovation Union flagship initiative which frames current EU research and technology development policy and integrates it into the broader context of the Europe 2020 strategy.

The Innovation Union in general

What is the definition of and rationale for innovation?

There is no one single definition of innovation. But innovation as described in the Innovation Union plan broadly means change that speeds up and improves the way we conceive, develop, produce and access new products, industrial processes and services. It implies changes that create more jobs, improve people's lives, and build greener and better societies.

Europe faces an innovation emergency. The best scientific and business brains are needed to face the challenges and seize the opportunities that lie in Europe's future. To keep pace with global competition and safeguard Europe's unique socio-economic model, Europe has to become more competitive and more innovative.

Therefore, in October 2010, the Commission proposed the Innovation Union flagship as one of the 7 flagship initiatives of the Europe 2020 strategy; it is an integrated innovation strategy of 34 specific commitments. The strategy aims to improve the conditions of access to finance for research and innovation in Europe, and to ensure that innovative ideas can be turned into products and services that create growth and jobs.

What is the Innovation Union?

The Innovation Union is a key element in the effort to achieve the goals of the Europe 2020 strategy for a smart, sustainable and inclusive economy.

The Innovation Union focuses on major areas of concern for citizens, such as climate change, energy efficiency and healthy living. It pursues a broad, balanced concept of innovation, both technological—leading to efficiency gains in production processes and improved performance of products—and concerning business models, design, branding and the services that add value for users. It includes public sector and social innovation as well as commercial innovation. It aims to involve all actors and all regions in the innovation cycle.

The policies in the Innovation Union plan aim to do three things:

- make Europe a world-class science performer;
- revolutionise the way public and private sectors work together, notably through Innovation Partnerships;
- remove the bottlenecks such as expensive patenting, market fragmentation, slow standard-setting and skill shortages that currently prevent ideas from getting to the market quickly.

A fundamental principle of the Innovation Union is that innovation is everyone's business and should become the overriding objective in economy-wide approaches. Such a strategic approach can only happen with high-level steering and when all actors take collective responsibility for its delivery.

The Innovation Union also introduces the strategic use of public procurement budgets to finance innovation, a comprehensive innovation scoreboard based on 25 indicators, and a European knowledge market for patents and licensing.

It includes measures to reinforce successful existing initiatives such as the Risk Sharing Finance Facility (RSFF), which has so far attracted stakeholder funding 15 times greater than the combined Commission and European Investment Bank (EIB) contribution of over €1 billion. Another

central element concerns the measures taken to revitalise and speed up efforts to build a European Research Area (ERA).

The Innovation Union proposes that the EU and its Member States will have to put into place integrated policies to ensure that the best academics, researchers and innovators reside and work in Europe. Furthermore, the possibilities made available under the Scientific Visa Package and the Blue Card scheme are to be used to attract a sufficient number of highly skilled third-country nationals to stay in Europe for limited periods.

It also seeks to refocus R&D on such major societal challenges as climate change, energy efficiency, health policy and demographic change. The shared ambition of the EU and its Member States is to put in place a new environment for innovation—one that is based on a framework for business that promotes and rewards innovation, leverages more private investment and attracts top talent from around the world.

Why Europe has to become an Innovation Union

Boosting Europe's research and innovation performance is the only way for Europe to support sustainable growth and create good and well-paid jobs that will withstand the pressures of globalisation. Currently, Europe has many strengths but is in danger of lagging behind the US, while other countries are catching up fast.

Europe is spending 0.8% less of its gross domestic product (GDP) on R&D than the US every year and 1.5% less than Japan. Europe has not yet achieved its target of investing 3% of GDP in research and innovation; rather, the current rate is under 2%.

Raising investment in R&D to 3% of the EU's GDP is one of the five priorities of the Europe 2020 strategy. This target is for the EU as a whole and is based on 1% public investment (a target already met or nearly met in many Member States) and 2% private investment (a target nowhere near

met in most Member States; the gap in private investment is about €100 billion).

Achieving Europe's target of investing 3% of EU GDP on R&D by 2020 could create 3.7 million jobs and increase annual GDP by €795 billion by 2025. To be able to reach this target, Europe would require at least one million more researchers in the next decade.

Private sector R&D is increasingly outsourced to emerging economies, and thousands of Europe's best researchers and innovators have moved to countries where conditions are more favourable.

Although the EU market is the largest in the world, it remains fragmented and insufficiently innovation-friendly. Too few of Europe's innovative small and medium-sized enterprises (SMEs) grow into large, globally successful companies.

What are the main obstacles to innovation in Europe?

There are two main obstacles:

- Unfavourable framework conditions: private investment in research and innovation is being held back and ideas prevented from reaching the market by the poor availability of financing, costly patenting, market fragmentation, outdated regulations and procedures, slow standard-setting and the failure to use public procurement strategically.

- Fragmented effort: national and regional research and innovation systems are still working along separate tracks, leading to costly duplication. By better pooling our efforts and focusing on excellence, and by creating a true ERA, the EU can enhance the quality of research and Europe's potential for major breakthroughs. And through Innovation Partnerships and other measures, the EU can rebuild broken links in the chain, bridging the gap between research and the market.

How can Europe invest in the Innovation Union in times of crisis?

Europe has to innovate to get back on the path to growth and jobs, but the continent is going through very tough times. Economic recovery has stalled and public confidence has deteriorated. The pressure to cut investments in future sources of economic growth is huge.

In times of austerity, fiscal consolidation is a necessity. However, to emerge from the current crisis stronger, the fiscal consolidation must be 'smart' in order not to jeopardise future growth. 'Smart' means preserving and reinforcing investments in sources of future growth—education, research and innovation—while increasing efficiency and carrying out structural reforms. This is of crucial importance in the context of increased competition at a time when the global quest for knowledge is intensifying.

The Organisation for Economic Co-operation and Development (OECD) and others have strongly urged governments to maintain and increase research and innovation investments, even in difficult times, because these are pro-growth, anti-crisis investments. The Commission shares this position, and the Innovation Union Communication[3] makes it clear that investments in research and innovation will have to speed up economic recovery, create jobs and improve European competitiveness.

But the Innovation Union is not only about investing public money; it is above all meant to better use public money to boost private sector investment and to put smarter regulations in place to drive innovation. Given the need for value for money, the Innovation Union aims to avoid costly duplication and overlap by pooling efforts and expertise on research and innovation.

Innovation Union and Horizon 2020

Through the Europe 2020 strategy and its Innovation Union flagship initiative, the political context for the EU's research and innovation policy

has now been firmly set for the years to come. A strong focus on tackling societal challenges through more impact and innovation will be key to delivering on Europe 2020. In addition, this new policy context puts a strong emphasis on creating socio-economic impact through innovation.

Horizon 2020 is designed against this backdrop and should be able to deliver more effectively than its predecessors on these aspects.

Its proposed budget breakdown reflects the challenges that Europe is facing and gives a prominent role to three main blocks of activities:

- A proposed €27.8 billion is intended to raise the excellence of Europe's science base. This is crucial to generating the innovation needed to sustain Europe's competitiveness in the long term. It is to be achieved through initiatives supporting frontier research (European Research Council), future and emerging technologies (FET), Marie Curie Actions and priority research infrastructures.

- The sum of €20.3 billion is to be used to support Europe's industrial base to make Europe a more attractive place to invest in R&D. Related initiatives will include increasing investment in enabling and industrial technologies, facilitating access to risk finance and providing EU-wide support for innovation in SMEs.

- The sum of €35.8 billion is to be spent on tackling societal challenges. This is in line with the key policy objectives of Europe 2020, which aim to turn the challenges of today into the business opportunities of tomorrow. This priority would support activities across an entire spectrum, from research initiatives to the market. Its focus will be on the challenges of health, demographic change and well-being; food security and the bio-based economy; secure, clean and efficient energy; smart, green and integrated transport; a supply of raw materials; resource efficiency and climate action; and inclusive,

innovative and secure societies. The European Institute of Innovation and Technology (EIT) would, through its Knowledge and Innovation Communities (KIC), contribute to addressing these challenges.

These amounts are complemented across all priorities by those dedicated to supporting the EIT, for which total funding of approximately €3.2 million has been proposed by the European Commission. Furthermore, the Joint Research Centre (JRC) will continue its role in contributing scientific expertise to the Union's policymaking process.

Horizon 2020 will be designed on the following pillars, coupling research with innovation in ways never experienced before:

- It will take a broad approach to innovation that is not only limited to bringing new products to the market but which also covers processes, systems or other approaches for non-commercial applications such as those intended for better public services or for addressing social needs (social innovation). It will also include initiatives emphasising European strengths in design, creativity and services, and the importance of social innovation.

- Stronger support will be given to the market uptake of innovation (including by the public sector), which will lead to more proof-of-concept, piloting and demonstration. It will involve a better use of the potential of research infrastructures, as well as mechanisms for setting technical standards, pre-commercial procurement and strengthened loan and equity financing. It will also strengthen bottom-up activities and launch inducement prizes to encourage different types of innovators to feel involved through rewards.

- Horizon 2020 will include major simplification through simpler programme architecture, a single set of rules, less red tape through an easy to use cost-reimbursement model, less paperwork in preparing proposals, fewer controls and audits, and a single point of access for participants.

- As a single programme, Horizon 2020 will promote the exchange of ideas and perspectives by deploying a seamless approach, allowing participants to move swiftly between different parts.

Implementation will be simplified and standardised, and simplification will cover both funding schemes and rules. Key aspects will include a rationalised set of funding schemes, a single set of rules, earlier project starts and major externalisation.

Horizon 2020 will be a break with the past, but it will also provide continuity with those programmes which are currently proving to be particularly successful, such as the European Research Council, the Marie Curie Actions, the EIT mission and the collaborative research actions.

The Innovation Union in detail

Bringing good ideas to the market

How will the Innovation Union enhance access to finance?

The Innovation Union aims to release private sector investment and proposes, among other things, to increase European venture capital investments, which are currently at a quarter of the level of those in the US. Current EU schemes show that a contribution from the EU budget can leverage more than 20 times the amount of investment from private capital. The Commission proposes scaling up these successful schemes and creating a regime to allow cross-border Venture Capital Funds.

The Commission will strengthen the cross-border matching of innovative firms with suitable investors. In addition, in the context of the SME Finance Forum, the Commission will focus, *inter alia*, on the particular financing problems faced by small, innovative companies.

Furthermore, the RSFF is a credit risk-sharing scheme jointly set up by the Commission and the EIB. Its purpose is to improve access to debt financing for private companies or public institutions promoting R&D and innovation activities which could yield major public benefits but which have a financial risk profile that may deter private investors in the absence of public backing. It was set up by the European Commission and the EIB. To date, contributions for the RSFF of €430 million from the EU budget and €800 million from the EIB, as risk-sharing partners, have supported over €18 billion in investments (15 times the combined contribution to the RSFF and 42 times the EU budget contribution).

The Competitiveness and Innovation Programme (CIP) financial instruments cover loan guarantees and venture capital and are managed by the European Investment Fund (EIF), whose majority shareholder is the EIB. To date, the €400 million contribution to the CIP financial instruments up to the end of 2009 has leveraged investments of €9 billion (22 times the budget contribution), benefiting some 68,000 SMEs.

Working with the EIB, the Commission has proposed the scaling up of both the RSFF and the CIP. The Commission is also working on further proposals with the European Investment Bank Group, national financial intermediaries and private investors to address investment in knowledge transfer and start-ups, and to guarantee venture capital for fast-growing firms expanding on EU and global markets.

With respect to the Structural Funds, these already provide substantive investments in research and innovation; some €82 billion have been programmed for the current financing period, of which large amounts still remain unspent. These remaining funds could be used to maximise effects for innovation and to achieve the Europe 2020 objectives. Under the next programming period (2014–20), Structural Funds should be increased and spent more effectively.

Innovation Union creating a single market for innovation

The EU market is the largest in the world; unfortunately, however, it is too often one of fragmented national markets with costly procedures. The

Innovation Union proposes the creation of a genuine single market for innovation which would attract innovative companies and businesses. To achieve this, several measures have been proposed in the fields of patent protection, standardisation, public procurement and smart regulation.

Smart regulation can be a key driver for innovation, in particular when dynamic and market-based approaches are used.

The Innovation Union recommends that the European Parliament and the Council take the necessary steps to adopt the proposals on the EU patent, including on the language regime, so that the first EU patents can be delivered in 2014. An EU patent alone would save innovative businesses an estimated €250 million.

The development of common standards is essential. Today, innovation cycles have become much shorter than the time it often takes to develop a European standard. These deficiencies have wide ramifications for the EU's position in global markets. A legislative proposal on standardisation should be developed which would speed up standard-setting to enable inter-operability and foster innovation in fast-moving global markets.

Public procurement accounts for some 17% of the EU's GDP. This represents an important market for innovation, particularly in areas such as health, transport and energy. To create procurement markets across the EU, with funds of at least €10 billion a year for innovations that improve the efficiency and quality of public services, Member States and regions are to set aside dedicated budgets for pre-commercial and public procurements of innovative products and services. This refers to procurements of R&D services (pre-commercial procurement) and of new technologies and innovations as identified by the European Innovation Partnerships. The goal is to increase these levels over time towards the level in the US, which is about $50 billion per year.

Some of the concrete measures that have been explored to create a single market for Innovation will have direct benefits:

- By adopting the European patent, it will be easier, quicker and cheaper to protect intellectual property by EU unitary patent, saving up to 80% on the current cost.

- By reforming the European standardisation system, the creation of standards will be faster and more efficient, especially in the information and communication technology (ICT) sector.

- By lifting legal and administrative hurdles, cross-border venture capital funds can be raised freely throughout the EU and invested in innovative SMEs.

- By improving the use of budgets for public procurement, the take-up and use of innovative products through pre-commercial and first commercial procurement of innovation will be promoted.

European Innovation Partnerships

European Innovation Partnerships (EIPs) are a new approach to EU research and innovation. They each tackle a specific societal challenge that is shared across the EU and that represents a large new market potential for EU businesses.

EIPs have clear and measurable goals and will bring the benefits of innovation to European citizens as rapidly as possible. They provide frameworks for mobilising actors across the innovation cycle and across sectors, with the intention of speeding up innovative solutions to societal challenges in order to:

- step up research and development efforts;

- coordinate investments in demonstrations and pilots;

- anticipate and fast-track any necessary regulation and standards; and

- mobilise demand, in particular through the better coordination of public procurement, to ensure that any breakthroughs are quickly brought to market.

Each partnership is led by a representative steering board chaired by the European Commissioner or Commissioners with lead portfolio responsibility for the policy area or areas concerned. A secretariat is provided by the Commission. The Board is to be composed of a limited number of high-level representatives from Member States (Ministers), Members of the European Parliament, industry leaders, researchers and other key stakeholders. The Board's first task is to draw up a multi-annual strategic work plan containing concrete targets and research and demand-side activities, and which assesses funding requirements, allocates responsibilities and defines the milestones to monitor progress.

All stakeholders involved in a Partnership will be expected to contribute to its financing; the Commission will seek to leverage the EU budget to provide 'seed' money.

Public–Private Partnerships

To achieve sustainable growth in Europe, the contribution of public and private players is indispensable. Responsible research and innovation requires that the best solutions be derived from interactions between partners that have various perspectives but common interests. As industry represents 66% of the private expenditure on R&D in Europe, Public-Private Partnerships (PPPs) have been established under the Seventh Framework Programme for Research, Technological Development and Demonstration (FP7). Some of the existing PPPs have been based on a contractual arrangement between public and private actors, and others have been set up as institutionalised PPPs (such as Joint Technology Initiatives and other Joint Undertakings).

The PPPs have provided the means to identify and to solve problems together with industry by facilitating the prioritisation of research and innovation in line with industry needs. Based on research and innovation

agendas defined by industry and business with the research community, PPPs have successfully supported research development and demonstration activities. Thus, they have helped to strengthen European industrial leadership. More important, they have also exercised a leverage effect on the research and innovation investments made by European industry.

Europe cannot afford to refrain from these combined activities if we want to promote a research-intensive and innovative Europe. For research to succeed, it has to be promoted on a European scale. A highly globalised world contains many challenges for European industry with competition from both rapidly developing countries and more traditional industrialised countries. Individually, European companies face problems in realising the costly research investments necessary to achieve technological breakthroughs.

Standardisation is often also linked with this kind of cooperation, and this helps to facilitate the market uptake of research results. Therefore, increasingly more companies in different sectors are seeing the advantages of working together in PPPs, allowing the EU to grow faster and stronger. In addition, PPPs facilitate the participation of SMEs in EU-funded research initiatives.

Investing public money in PPPs can, however, only be justified if, in addition to the leverage effect, the societal challenges which respond to citizens' needs are addressed. PPPs, therefore, will have to present clear visions with quantified objectives. For example, efficiency improvements in CO_2 equivalent footprints of up to 40% will have to be met by 2030 for the sustainable process industries to meet the climate change challenge.[4] Another example, here with regard to the health challenge, is that new antibiotics need to be developed by the pharmaceutical industry, as no new antibiotics have entered the market in quite some time, despite the fact that antibiotic resistance is increasing dramatically.[5]

Against this background, Horizon 2020, the new Framework Programme for Research and Innovation proposal, states that, through PPP, all partners concerned commit to supporting the development and implementation of research and innovation activities of strategic importance to the Union's

competitiveness and industrial leadership, and to addressing specific societal challenges.

Existing PPPs may receive support from Horizon 2020, provided that they address Horizon 2020 objectives, they meet the criteria laid down in Horizon 2020 and they make significant progress under FP7. The following are Joint Undertakings established in FP7 under Article 187 of the Treaty Founding the EU, for which further support may be provided under the above conditions: the Innovative Medicines Initiative (IMI), Clean Sky, Single European Sky ATM Research (SESAR), Fuel Cells and Hydrogen (FCH), embedded computing systems (ARTEMIS), and nano-electronics (ENIAC). The latter two may be combined into a single initiative.

The following are Contractual PPPs supported under FP7 that might receive support under Horizon 2020 if the above conditions are met: Factories of the Future, Energy-efficient Buildings, European Green Cars Initiative and Future Internet. Further support may also be provided to the European Industrial Initiatives (EIIs) established under the European Strategic Energy Technology Plan (SET Plan).[6]

Following the strong interest manifested by several industrial sectors, new PPPs may be launched under Horizon 2020 if they meet the defined criteria. These may include partnerships concerning ICT in the areas of photonics and robotics, sustainable process industries and bio-based industries.

The Commission will ensure openness and transparency in the selection process and in clarifying industry's commitments and the leverage effects of the PPPs. The Commission is confident that PPPs offer an excellent instrument for mobilising significant public and private resources to increase Europe's research and innovation capacity.

More efficient EU, national and regional innovation systems

The success of the Innovation Union depends largely on the dynamism and effectiveness of national and regional innovation systems and, in

particular, on efforts to draw synergy effects from closer cooperation between Member States and closer alignment with EU priorities. Increasing the EU's innovation capacity in the context of a tight budgetary context is a tremendous challenge.

A world of opportunities

International cooperation must go hand in hand with an integrated approach to facilitating the bringing of the results of common R&D and innovation projects to the market.

The Innovation Union proposes that the EU and the Member States treat scientific cooperation with third countries as a matter of common concern and mutual benefit. Common approaches—notably on intellectual property protection and standardisation—should be developed with third-country partners. This would contribute to the development of global approaches and solutions to societal challenges and to the establishment of a level playing field.

In 2012, the adopted policy framework for international cooperation in research and innovation aimed to reach an agreement with international partners on the development of research infrastructures which, given their cost and complexity, can only be developed on a global scale.[7] The Innovation Union recommends that, by 2015, Member States, together with the Commission, complete or launch the construction of 60% of the priority European research infrastructures currently identified by the European Strategy Forum for Research Infrastructures (ESFRI).

Innovation Union and the ERA

The Innovation Union aims to foster a well-functioning ERA in which researchers, scientific knowledge and technology can circulate freely. As a result of the European Council conclusions of 4 February 2011, Member

States committed to completing the ERA by 2014.[8] The Commission launched a stakeholder consultation on 13 September 2011 and on 17 July 2012 adopted the Communication *A Reinforced European Research Area Partnership for Excellence and Growth,*[9] which set out a non-legislative approach based on reinforced partnership between the Commission, Member States and research stakeholder organisations.

Since the creation of the ERA in 2000, a lot of progress has been made in five main areas: human resources, research programmes, research infrastructures, knowledge transfer, and international science and technology cooperation. But Europe's researchers, research institutions and funding agencies still face major legal and technical obstacles preventing them from working and operating freely, especially across borders. The new ERA framework will now implement supporting measures to remove these obstacles.

The end of 2014 is the deadline that has been set by the Innovation Union for achieving a genuinely unified ERA in which all actors, both public and private, can operate freely, forge alliances and gather critical mass in order to compete and cooperate on a global scale.

The Innovation Union's achievements to date

A key milestone in the implementation of the Innovation Union was reached at the 4 February 2011 European Council meeting, at which the heads of state and government gave their strong backing to a series of proposals in the Innovation Union, set priorities and lent the necessary political momentum for innovation-driven change through a shared European agenda.[10]

No time was lost in taking action. The first year of implementation of the Innovation Union flagship initiative involved the launch of several pilots to explore and test, on a smaller scale, new activities such as the EIP and to gauge future support for public procurement of research and innovation.

Wide debates with stakeholders were organised across different Innovation Union commitments, ranging from the future of EU research and innovation funding to the modernisation of EU public procurement legislation. Such discussions and testing were critical to ensure that the Innovation Union actions were designed and implemented in the best possible way with efficient use of resources. They also allowed all stakeholders to have a say in how to build the Innovation Union.

In June 2011, the Commission concluded the first ever 'European semester' by putting forward a policy guidance package of country-specific recommendations and recommendations for the euro area. For research and innovation, it concluded that there is a need for additional efforts in order to achieve the EU 3% R&D target and for a call for smart fiscal consolidation. Overall, Member States are required to consider how to prioritise expenditure on research and education and the key infrastructures that are needed to sustain growth, while maximising the quality of spending and efficiency of services.

An extensive public consultation on future EU research and innovation funding also took place in the first half of 2011. It showed strong support for bringing together all EU research and innovation funding under a common strategic framework, providing simplified and seamless support across the full innovation cycle to increase impact. In the Commission's proposal for the next EU budget, investment in research and innovation is set to increase by 46% in real terms. The corresponding legislative proposal for the programme, Horizon 2020, was adopted on 30 November 2011.

What has been achieved up to now?

Good progress has been made in launching and implementing 30 out of the 34 Innovation Union commitments. Notably, by the end of 2011, based on wide stakeholder consultations, the Commission had put forward six

legislative proposals announced in the Innovation Union. These proposals will bring a major change in framework conditions for innovation in Europe.

The Innovation Union set out specific proposals on how to remove the remaining barriers for innovative businesses to turn ideas into commercial successes. According to the Communication approved on 2 December 2011, *State of the Innovation Union 2011*, actions are moving ahead, allowing for better access to capital, faster and modernised standard-setting, more affordable patents, more public procurement of innovative products and services, and so on.[11] The following are among the most notable achievements:

- A public consultation was launched in June 2011 on the core elements for a new regime for venture capital. By the end of 2011, the results had been taken up in a Commission proposal which aims to enable the true integration of the venture capital market in Europe and to strengthen the supply of venture capital.

- In June 2011, the Commission presented a standardisation package with the aim of updating European standardisation legislation and policy as a means to face present and future challenges and to better support innovation.

- On 11 December 2012, the European Parliament adopted the legislative proposals creating a unitary European patent under enhanced cooperation from 25 Member States. This will reduce the costs of patents in Europe by up to 80%.

- Pilot calls for proposals were launched under FP7 and CIP. A feasibility study was also initiated to explore designs for a support scheme for public procurement of research and innovation.

- The conditions were established for an EU-wide knowledge market aimed not only at facilitating the exploitation of knowledge but also at giving rise to important new sources of revenue which can be

reinvested in research and innovation. The Commission presented a standardisation package, which aims to modernise European standard-setting in order to face present and future challenges. The target is to speed up standard-setting processes by 50% by 2020.[12]

By now, the Commission has piloted the first EIP in the area of active and healthy ageing. This pilot partnership aims to add two healthy years to our average lifespan. The Strategic Implementation Plan of the pilot partnership was presented in November 2011. The experience gained in setting up this pilot will pave the way for other partnerships. On 29 February 2012, the Commission adopted the Communication, *Taking Forward the Strategic Implementation Plan of the European Innovation Partnership on Active and Healthy Ageing.*[13]

Recently, other EIPs have been set up on agricultural productivity and sustainability, raw materials, and water, as well as on smart cities and communities. They target specific priorities, such as agriculture, the raw materials value chain, water management and urban services, in order to develop joint solutions from the scientific community, public authorities and the business sector. Through a common platform, partnerships aim to promote cooperation between science and industry as well as innovative practices for testing and applying new technologies, processes and products.

There has been a good track record on putting in place the conditions that will smooth the path from idea to market and boost private investments in research and innovation.

To better integrate the innovation cycle, EIT brings together higher education institutions, research organisations and businesses in new types of partnerships—KICs—operating in the areas of sustainable energy (KIC InnoEnergy), climate change adaptation and mitigation (Climate-KIC) and future information and communication society (EIT ICT Labs).

On 30 November 2011, the Commission adopted a proposal for EIT's Strategic Innovation Agenda which defines the framework for the Institute's

operations in the years to come. It focuses on consolidating the three existing KICs and gradually setting up new ones, which will address major societal challenges in line with the Horizon 2020 objectives.

Key milestones have been reached on many other Innovation Union commitments. For example, in 2012, the Social Innovation Europe initiative was launched in March and a Smart Specialisation Platform was released in June. A European Design Leadership Board has been set up. A pilot project for Knowledge Alliances between business and academia has been launched. The European Commission has also piloted an EU-level mechanism of support for public procurers.

Although many milestones have been reached, much is still to be done. In particular, efforts have to be stepped up at the national level to prioritise investments in research and innovation and to set aside dedicated budgets for the public procurement of innovative products and services in the interests of driving demand for innovative solutions. The Commission will also step up efforts to issue an eco-innovation action plan and screen the regulatory framework in key areas.

What is to be achieved under Horizon 2020?

The Commission has proposed increasing investments in research, innovation and education in support of the EU's pro-growth agenda. Horizon 2020, the new €80 billion investment programme for research and innovation, brings together all existing EU research and innovation funding and provides support in a seamless way from idea to market. This will be achieved through streamlined funding instruments and the implementation of simpler programme architecture and rules for participation.

Horizon 2020 enacts many of the specific Innovation Union commitments, notably by focusing on societal challenges, simplifying access, involving SMEs, strengthening financial instruments, supporting

public procurement of innovation, facilitating collaboration, and supporting research on public sector and social innovation.

Furthermore, the future Cohesion policy will have an increased focus on research and innovation. In more developed regions, at least 80% of resources from the European Regional Development Fund at the national level will be allocated to innovation, together with the priorities on fostering a low-carbon economy and competitive SMEs. This amount will be 50% in less developed regions. In line with a more strategic focus, the support will be conditional on the existence of a national or regional strategy for smart specialisation.

In addition, the proposed Programme for the Competitiveness of Enterprises and SMEs (COSME Programme) will focus on providing financial instruments and support for the internationalisation of enterprises. The Programme is expected to assist 39,000 firms yearly, helping them create or save 29,500 jobs and launch 900 new business products, services and processes.

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Michael Hager

Energy Policy at the Centre of European Policy

Introduction

Energy policy has moved to the centre of European politics in recent years. The security of the energy supply is increasingly viewed with concern in light of rising electricity, gas and fuel prices, as well as acute natural gas supply crises. The price gap for electricity and raw energy commodities between Europe and its competitors is widening. The debate about global warming and the urgent need to reduce CO_2 emissions has made the importance of an environmentally friendly energy supply a core public interest. We will become ever more dependent on energy imports in the next few decades. Significant efforts will therefore be required to maintain the current security of the energy supply in the future while meeting our ambitious climate protection targets.

Changes in our energy consumption and the markets underscore the need for an ever-evolving energy policy. World energy use continues to increase at approximately the same rate as the gross domestic product and will have to account for the growth in the global population to 8 billion people by 2030. Oil prices have fluctuated greatly, reaching a peak of $150 per barrel in the summer of 2008 but falling dramatically as a result of the financial crisis. Gas and coal prices have similarly undergone considerable change over the past decade as a result of the shale gas revolution in the US. Climate politics has become synonymous in the mind of the European public with energy politics, and renewable and non-polluting energy sources are developing rapidly to accommodate new needs for low-carbon energy production. Also, the disaster at Fukushima has led to a reflection on nuclear power, notably resulting in Germany's decision to phase out nuclear energy as part of its *Energiewende*.

Against this background, with the start of the Barroso II Commission in 2009, a new European Energy Policy has been set out under the responsibility of Commissioner for Energy, Günther Oettinger. In November

2010, the Commission adopted its Communication, *Energy 2020: A Strategy for Competitive, Sustainable and Secure Energy*, setting out the major priorities for a truly European energy policy, friendly to consumers, industry and the environment, under the threefold objectives of security of supply, competitive pricing and sustainability.[1] The Commission is working to ensure the full implementation of the Third Energy Package's network unbundling provisions, complete an interconnected European energy market, and create a competitive sector that delivers energy prices comparable with those of industrial and fast-developing competitors around the world. The Commission prioritises the need to provide affordable energy so that European industry can compete on the world stage and ordinary household consumers can afford to pay their bills.

For security of supply, the Commission is seeking to diversify sources of raw energy commodities and electricity, including increasing the proportion of electricity derived from renewables and forming partnerships with third-country suppliers of gas and oil. Within the domain of sustainability, the '20-20-20' initiative remains in place: this mandates that, by 2020, greenhouse gas emissions be reduced by 20%, the share of renewables in final energy consumption be increased by 20% and energy savings be increased by 20%. In December 2011, the Commission adopted its *Energy Roadmap 2050*, which analysed various scenarios for reaching the EU's 2050 goal of 80% reduction in CO_2 emissions, providing greater certainty to investors on decarbonisation policy at a time power infrastructure, built 30 or 40 years ago, is in the process of being replaced.[2]

At the level of the European heads of state and government, energy is also recognised as an important topic, as reflected in the conclusions of the European Council of February 2011, which clearly supports the Commission on the way to a truly European energy policy.[3]

The present document details some of the most important measures to these ends and discusses the progress that the Commission has made towards creating a competitive, sustainable and secure energy supply for all of the EU.

Reducing energy demand and promoting energy savings

Enshrined as the third pillar of the 20-20-20 initiative, energy efficiency is the most immediate and cost-effective way of addressing the EU's strategic security of supply and competitive economic and decarbonised energy objectives, while providing average savings to households of up to €1,000 per year. On 25 October 2012, the EU adopted the Energy Efficiency Directive, establishing a common framework of measures for the promotion of energy efficiency within the EU.[4] It lays down rules designed to remove barriers in the energy market and overcome market failures that impede efficiency in the supply and use of energy, and provides for the establishment of indicative national energy efficiency targets for 2020. Specific programmes within the domain of energy efficiency policy in the EU include the following:

- *Financing energy efficiency.* Financial support is available through various EU programmes and instruments which aim to assist Member States in supporting EU policy implementation and initiating associated investments. These include the European Energy Efficiency Fund (EEEF), with a global volume of €265 million, which provides tailor-made debt and equity instruments to public authorities for the promotion of energy-efficiency measures.

- *Energy efficiency of buildings.* Buildings account for 40% of the total energy consumed in the EU, and the sector has significant untapped potential for cost-effective savings which could amount to 11% of final energy use in 2020. In order to attain some of these savings, the EU adopted the Energy Performance of Buildings Directive in May 2010, obliging Member States to establish and apply minimum energy performance requirements for new and existing buildings, ensuring the certification of building energy performance, and requiring the regular inspection of boilers and air-conditioning systems in buildings. The Directive also requires Member States to ensure that, by 2020, all new buildings are 'nearly zero-energy buildings'.

- *Energy efficiency of products.* The energy demand of households accounts for 25% of final energy needs in the EU. The EU seeks to improve efficiency in this sector in two complementary ways: energy labelling of household appliances and Minimum Efficiency Requirements. The EU's Energy Labelling Directive was adopted in May 2010 and mandates the use of labels that rate energy efficiency, helping consumers choose products that save energy and money, thus providing incentives for industry to develop energy-efficient product design.[5]

The 2012 Directive also requires public bodies to buy energy-efficient products and services and refurbish 3% of their buildings each year to reduce their energy consumption. It also requires energy utilities to encourage end-user to cut their energy consumption through efficiency improvements such as the replacement of old boilers or insulation of their homes, and requires large companies to undertake audits on energy efficiency every three years. The Commission will continue to oversee implementation of these measures at Member State level.

Building a truly pan-European integrated energy market for more affordable and secure energy supplies

The EU aims to fully integrate national energy markets by 2014, to give households and businesses more and better products and services, more competition, and more secure supplies, as well as to give Europe a stronger bargaining position on the international level. In turn, this integration will result in lower end-prices for all consumers. Progress has already been made: consumers can switch suppliers for gas and electricity faster and in many more countries than was possible 10 years ago, and suppliers now have a much greater obligation to provide clear explanations of terms and conditions. Work still to be done includes aligning national market and network operation rules for gas and electricity, as well as making cross-border investment in energy infrastructure easier.

To achieve the goal of the internal market, a host of legislative proposals have already been adopted. Among the most significant, the European Commission adopted the 'Third Package' of legislative proposals for the electricity and gas markets, which entered into force in March 2011.[6] This mandates

- the separation of production and supply from transmission networks (unbundling) in order to enhance competition in energy supply and create incentives for companies to invest in new infrastructure;

- the creation of a cross-border agency, the Agency for the Cooperation of Energy Regulators (ACER), to increase exchange between national energy regulators and thus ensure proper handling of cross-border energy transmission;

- the strengthening and guaranteed independence of national regulators;

- the establishment of the European Network of Transmission System Operators for cross-border collaboration, one for gas (ENTSO-G) and one for electricity (ENTSO-E);

- the creation of a regulatory framework to support the single energy market by developing network codes, a legally binding set of common technical and commercial rules and obligations that govern access to and use of the European energy networks, to be developed by the ENTSOs; and

- greater access to information on energy markets and network operation, and more Europe-wide solidarity in the face of energy supply threats.

To keep this at the top of the European agenda in the current term, Commissioner Oettinger led the publication of the Commission's Internal Energy Market Communication in November 2012. The Communication sets

out the state of play and progress of the internal market to date, with individual analysis for each of the 27 Member States, and provides a detailed Action Plan to ensure full achievement of the market by the end of 2014.[7] The Communication encourages Member States to step up efforts to transpose and implement their obligations under the Third Package, highlighting the benefits of a truly integrated European market for citizens and business. The document identifies the need for further action in a number of key areas, including consumer protection, bridging the gaps between the market development of different Member States, enforcing existing rules, and investing in the modernisation and extension of energy infrastructure. The EU will continue to play the leading role in ensuring follow-up of the findings presented in the Communication. Some of the main areas for progress are detailed below.

Protecting vulnerable consumers. Because the provision of secure, safe, sustainable and affordable energy supplies to EU businesses and households is at the centre of EU energy policy, the internal energy market and the 2012 Communication maintain a close focus on consumer protection. The energy market legislation sets high standards for consumer protection, and the liberalisation of gas and electricity markets are the basis for creating greater choice and price competition that consumers can tap into. The EU has to educate consumers about their rights, enforce the provision of clear billing, and provide transparent and comparable pricing systems and single points of contact in order to enable members of the public to maximise the benefits they receive from the liberalised and unified market. The Commission supports Member States in providing targeted assistance to vulnerable consumers and works directly with consumer organisations at the Consumers' Forum held annually in London.

Loop-flows. In spite of the benefits of the internal energy market, some problems have arisen which require new monitoring systems. A key example is the need to deal with loop-flows stemming from overcapacity on the German grid as a result of increased renewable input: electricity grid interconnections have made it possible for electricity to be routed through secondary Member States on its way back to the original generating country,

in this case through Poland and the Czech Republic. This can cause significant problems for the capacity of the secondary Member State's grid infrastructure. The Commission continues to bring together ACER and regulators from all affected countries to develop solutions to this problem.

Smart grids. As the Internal Energy Market Communication details, the long-term vision for the European internal energy market is also geared towards the full implementation of 'smart grids': bringing together the latest progress in information and communication technologies and network development to allow electricity to flow exactly where and when it is needed at the lowest cost. Smart grids will enable consumers to follow their electricity consumption in real time, saving energy and money. Estimates show that smart electricity grids should reduce CO_2 emissions in the EU by 9% and annual household energy consumption by 10%. They should also help ensure the secure functioning of the electricity system and enable the integration of vast amounts of renewables.

The Commission continues to monitor progress towards the implementation of the Internal Energy Market and will complete a full review of all points in the Action Plan in 2014. The Commission is committed to ensuring that the follow-up to the Action Plan at Member State and EU level be firmly anchored in the European semester, in particular via the country-specific recommendations.

Extending and modernising Europe's energy infrastructure

A further priority for the full achievement of the Internal Energy Market is the need for more and better energy infrastructure. The EU's infrastructure for gas, electricity and oil is ageing and not suited to meeting future energy demand or to taking up the rapidly increasing amounts of renewable energy as noted above. Significant investments for the realisation of a single European energy network are needed because of the financial and economic crisis, delays in permit-granting, lack of public acceptance of infrastructure,

and regulatory obstacles to cross-border cooperation, all of which demand a new approach to the way Europe manages and finances its networks.

In response to this need, the Communication on Energy Infrastructure Priorities, published in November 2010, identified a number of areas for improvement in the development of infrastructure for an integrated European energy market, such as faster and more transparent permit-granting procedures, stable financing frameworks, and the encouragement of cooperation through regional clusters such as the Baltic Energy Market Interconnection Plan (BEMIP) or the North Seas Countries' Offshore Grid Initiative.[8]

In October 2011, this Communication was followed up by the Energy Infrastructure Package, which aimed to facilitate cooperation on infrastructure creation across the EU. This sought to improve on existing European energy infrastructure policy over and above what was already in place as part of the Trans-European Network for Energy (TEN-E), which at the time provided limited funding to infrastructure projects along 12 strategic trans-European energy infrastructure corridors and areas. A new Regulation made a number of contributions to infrastructure policy, proposing a common method for the identification of 'projects of common interest' that are needed to allow the EU to meet its energy and climate objectives by 2020, and creating measures to accelerate their deployment by making permitting procedures more efficient and giving citizens the opportunity to participate in the planning process. This Regulation accompanied the Commission's broader Connecting Europe Facility, which proposed to fund €50 billion worth of investment for improving transport, energy and digital networks across Europe.[9] If the European heads of state and government agree, the energy sector might benefit from €9.1 billion for trans-European infrastructure, which will help close financial gaps and remove network bottlenecks. The money from the Connecting Europe Facility will act as leverage for more funding from other private and public investors.

The European Energy Programme for Recovery (EEPR) was established in 2009 to address both Europe's economic crisis and European energy

policy objectives. Almost €4 billion was assigned to co-finance EU energy projects that would boost the economic recovery, increase the security of the energy supply and contribute to the reduction of greenhouse gas emissions. The three sectors meeting these conditions were gas and electricity infrastructure, offshore wind energy, and carbon capture and storage projects. Fifty-nine energy projects received funding: 44 gas and electricity infrastructure projects, 9 offshore wind projects, and 6 carbon capture and storage projects.

Promoting renewable energy

In the decade to 2008, Europe's renewable energy industry faced limited and fragmented growth, partly as a result of a limited EU regulatory framework. Recognising that renewable energy should form the heart of any future low-carbon energy sector, the EU introduced a comprehensive and robust supportive legislative framework in 2009. The 2009 Renewable Energy Directive, which was to be transposed by Member States by December 2010, sets ambitious targets for all Member States as part of the 20-20-20 vision, such that the EU will reach a 20% share of energy from renewable sources by 2020 and a 10% share of renewable energy specifically in the transport sector. It also improves the legal framework for promoting renewable electricity, creates cooperation mechanisms to help achieve the targets cost-effectively and establishes sustainability criteria for biofuels.

To monitor progress towards these targets, the Directive required Member States to submit national renewable energy action plans by June 2010, with detailed roadmaps of how they expected to reach their legally binding targets, and progress reports by the end of 2011 and every two years thereafter.

In June 2012, Commissioner Oettinger provided a Communication on renewable energy, assessing progress towards the 2020 target of 20% of

energy use derived from renewable sources.[10] As part of its recommendations, the Communication encourages Member States to revise support schemes so that they are clearly framed, in order not to create confusion and engender negative consequences for investors. Moreover, it encourages the development of Member State private financing mechanisms that both attract capital and increase local acceptance of renewable energy projects.

Because the renewables infrastructure produces more energy where climatic factors are more advantageous, electricity grid interconnection between Member States—taking energy, for example, from places where there is more sunlight to where there is less—can contribute significantly to security of supply and competitive pricing. The Communication reinforces the importance of more coherent support schemes between countries in areas such as feed-in tariffs in order to reduce disparities which could act as barriers to transmission across national borders and to create a level playing field. It also places interconnection between the EU and the Southern Mediterranean high on the renewables agenda. The Commission continues to facilitate the development of cooperation mechanisms between Member States and will offer guidance in these areas in the course of 2013.

The Commission is also running a public consultation on capacity mechanisms between November 2012 and early February 2013. The variability of renewable energy production and the current absence of electricity storage technology create a new need for back-up energy generation when, for example, wind turbines are not turning or photovoltaic panels are not receiving enough solar energy. Some Member States have introduced or envisage introducing separate payments for generation capacity being available in the market, such as paying for the upkeep of a gas generator to be activated when other sources are not producing sufficiently. Such capacity mechanisms are long-term tools that aim to provide a stream of revenue to (selected) generators and commit consumers paying for the capacity provided. However, if capacity mechanisms are not well designed and/or if introduced prematurely or without proper coordination at EU level, the Commission believes that these mechanisms

risk being counterproductive. If they do not treat demand reduction fairly, they could lock in generation-based solutions rather than energy-efficient or demand-response solutions. Capacity mechanisms are also likely to favour fossil fuel generation sources over more variable renewable sources and may therefore contradict decarbonisation objectives and go against the optimisation of available EU resources. Poorly designed capacity mechanisms do not ensure generation adequacy or security of supply but rather distort investment signals. As such, these interventions can interfere with cross-border trade and competition, as they can close off national markets from generation elsewhere in the EU and distort the location of generation in the internal market.

Extending Europe's leadership in energy technology and innovation

Technological innovation is a fundamental part of delivering the sustainable, competitive and secure energy supply envisaged by the Energy 2020 initiative and the EU's longer-term energy policy. Without improved efficiency and new ways of dealing with carbon emissions, the bloc will almost certainly fail to meet its climate objectives and will face higher prices. The EU supports research for a broad portfolio of energy technologies: renewable energies (bio-, solar, wind, ocean, hydro- and geothermal), fossil fuels (for example, clean coal), electricity networks, energy efficiency, fuel cells and hydrogen, socio-economic research, materials, and future and emerging technologies. Key among these for the current Research Framework Programme (FP7, 2007–13) is research into carbon capture and storage (CCS), smart grids, energy efficiency, and nuclear technologies. The energy priorities in research feature in Horizon 2020, the new financial instrument for Europe's research agenda, which is to be agreed by the European Council.

Carbon capture and storage. The EU has supported the research, development and demonstration of clean coal and CCS technologies for almost 20 years. Under FP7, research and demonstration activities in the

field of clean coal technologies and CCS include advanced capture techniques, the qualification of deep saline aquifers, transport infrastructure, storage safety, public acceptance and feasibility/engineering studies for CCS demonstration plants. Such programmes are an important part of developing the confidence in CCS necessary to secure investors, in turn a key part of *Energy Roadmap 2050*.

Smart grids. To facilitate the transition to more sustainable energy systems, Smart Energy Networks are also one of the FP7 priority topics. Here the focus is on the efficiency, safety, reliability and quality of the European electricity and gas networks, notably within the context of a European energy market; the EU has supported Smart Energy Networks for more than a decade. Under the 6th Framework Programme (FP6, 2002–6), 27 projects were funded with an EU contribution of approximately €65 million. Thematic priorities were infrastructure (including ICT), microgrids and distributed generation.

Nuclear energy. FP7 Euratom aims to address the major issues and challenges in nuclear research, in both fission and fusion. To promote scientific research and technological development in the field of fusion, a Joint Undertaking for the International Thermonuclear Experimental Reactor (ITER) and the Development of Fusion Energy was established for a period of 35 years starting on 19 April 2007. Its members are Euratom, represented by the Commission, the EU Member States, and certain third countries which have concluded cooperation agreements with Euratom in the field of controlled nuclear fusion. Commissioner Oettinger continues to participate in high-level planning on research and investment in this project.

Completing the Community safety, security and non-proliferation framework for nuclear energy

Through the Euratom Treaty, the EU aims to ensure the safe and sustainable use of nuclear energy by developing and implementing a common EU legal

framework that meets the highest standards of safety, security and non-proliferation. It also aims to help countries outside the bloc to meet these standards.

After the nuclear accident in Fukushima, Commissioner Oettinger took the initiative to carry out Europe-wide safety checks of nuclear power plants. Supported by the European Council, the European Commission and the European Nuclear Safety Regulators' Group (ENSREG) agreed in May 2011 to undertake voluntary stress tests for the EU's 143 nuclear power reactors. These tests were based on a common methodology and assessed both natural and human-made hazards (for example, the effects of aeroplane crashes and terrorist attacks). The assessments were conducted by independent national authorities and through peer review, beginning in June 2011.

On 4 October 2012, the European Commission released its Communication on the results of the stress tests.[11] The document highlighted that European nuclear power plants have generally high safety standards but further improvements are needed in almost all of them, for example in executing periodic safety reviews and in assessing seismic and flooding hazards. The Communication details the specific needs of each Member State, as well as those of some neighbouring countries.

Dealing safely with nuclear waste is also a key concern for the EU and its Member States. Although low- and medium-level radioactive waste is increasingly being taken care of, there is not yet a single final repository for high-level radioactive waste and spent fuel. It is likely that the first repositories of this kind will be opened between 2020 and 2025 in several EU Member States. In July 2011, the Council adopted the Radioactive Waste and Spent Fuel Management Directive, proposed by the Commission in November 2010.[12] The Directive asks Member States to present national programmes, indicating when, where and how they will construct and manage final repositories that guarantee the highest safety standards. These safety standards will then become legally binding and enforceable in the EU. Member States must submit the first report on the implementation of their national programmes in 2015.

External supply security and the promotion of the sustainable use of energy worldwide

Given the EU's rising external supply dependence, the emergence of large new energy-consuming markets and volatile energy prices, external relations has become an integral part of the EU's energy policy. This area was given greater weight as a priority under the *Energy 2020* Communication, with a renewed emphasis on coordination at regional and Community level, in order to harness the collectiveweight of the 27 Member States when dealing with supplier countries and to avoid situations of many dialogues and contradicting messages with the same cooperation partner. In 2011, this priority was reinforced in the Communication *The EU Energy Policy: Engaging with Partners beyond our Borders*.[13] This set out a number of core priorities for the Commission's external energy action, including the strengthening of partnerships for secure, safe, sustainable and competitive energy, and the better promotion of EU energy policies beyond the Union's borders. Maintaining an ongoing energy dialogue with Russia, and developing projects with a view to diversifying energy sources, remain key in this regard.

Energy dialogue with Russia. Russia is the largest oil, gas, uranium and coal exporter to the EU. Likewise, the EU is by far the largest trade partner of the Russian Federation. Based on this mutual interdependency and common interest, the energy partnership within the EU–Russia Energy Dialogue, established in 2000, aims to improve investment opportunities in the energy sector to ensure continued energy production, to secure and expand transportation infrastructure, and to reduce the environmental impact. Following the 2009 gas dispute, the EU and Russia consider it essential to further reinforce mutual confidence by establishing an Early Warning Mechanism. This instrument ensures rapid communication and aims to prevent further supply interruptions in the field of gas, oil or electricity.

Southern Corridor and Nabucco. The Southern Corridor, linking the EU gas market directly to the largest deposit of gas in the world (the

Caspian/Middle East basin) would be—after the Northern Corridor from Norway, the Eastern Corridor from Russia, the Mediterranean Corridor from Africa and liquefied natural gas (LNG)—the fourth biggest source of gas for Europe. The diversification of sources generally improves competition and enhances the security of supply: as also seen in the January 2009 gas crisis, the most severely affected countries were those relying on one single import source. The implementation of the Southern Corridor requires close cooperation among several Member States, as no country individually requires the incremental gas volumes sufficient to underpin the investment in pipeline infrastructure. Therefore, the EU acts to promote diversification and provide security of supply for the public by bringing Member States and companies together in order to reach a critical mass.

Conclusion and outlook

The EU has made great progress on its path towards a more secure, competitive and sustainable energy sector. However, much is still to be done to ensure not only that the Union's goals are achieved for 2020 but also in the longer term. The EU remains committed to creating the energy conditions necessary for European growth, at the same time as reducing greenhouse gas emissions by at least 80% by 2050. *Energy Roadmap 2050*, published in 2011, outlines the approaches towards this goal while ensuring security of supply and price competitiveness, but there is a great deal of work ahead to ensure that these approaches are taken.

As we move closer towards the goals as outlined above, there is an ever-increasing need for more cooperation at the European level. Germany's *Energiewende* after the Fukushima disaster is an example of the challenges faced in this respect: Member States maintain their competency to decide their own energy mixes; however, their decisions now affect the security of the supply, infrastructure and pricing outside their own borders. Germany's rapid move towards more renewable energy creates uncertainty for neighbouring countries; the over- and undersupply of energy, varying

according to the amount of production in Germany, affects other Member States in line with supply to the German grid. Greater and earlier cooperation on energy policy reduces the risk of problems spilling over into other countries in the Union. This clearly makes the case for a further 'Europeanisation' of energy policy.

A modern—sustainable, secure and competitive—energy industry needs Europe to move forward together. As the EU seeks to secure a recovery from its long-running slump, it becomes ever more in need of a revival in industry, in trade, in entrepreneurship and in employment. All of these require a stable supply of energy at a competitive price. At the same time, Europe remains a leader in the fight to tackle climate change and, indeed, in the low-carbon technologies industry. It is important that it maintains this place. Energy policy is, therefore, already at the centre of European life. It ought also to remain firmly at the heart of European policy as a whole.

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Eveline Lecoqu

European Environmental Policy: Living Well, within the Limits of Our Planet

Introduction

Maintaining the environment as a priority is vital for the future of Europe, especially in this time of economic crisis. Our natural capital and the resilience of our ecosystems play an important role in ensuring long-term prosperity and well-being. Furthermore, moving towards a more inclusive and competitive green economy will offer new opportunities for economic growth and job creation.

In November 2012 the European Commission presented its proposal for a 7th Environmental Action Programme (EAP), to run until 2020. This is currently being reviewed by the European Council and Parliament. The proposal builds on the important achievements in the past 40 years of European environmental policy and provides an overarching framework for recent environment and climate policy initiatives. Its aim is to commit the EU institutions, Member States, regional and local authorities, and other stakeholders to a common agenda for environmental policy action. It will also contribute to implementing the smart, sustainable and inclusive growth agenda of the Europe 2020 Strategy and its flagship initiative 'A Resource Efficient Europe'. By establishing clear priority objectives for 2020, the 7th EAP proposal also lays the groundwork for the development of a long-term vision for 2050.

The main environmental challenges today

Since the early 1970s, a broad range of environmental legislation has been put in place, adding up to the most comprehensive set of modern standards in the world. This has helped to address some of the most serious environmental concerns of citizens and businesses in the EU.

Examples of the main environmental challenges to date are listed below, together with the most important recent policy initiatives addressing them.

Biodiversity loss and the degradation of ecosystems

Biodiversity, ecosystems and the services that they provide represent a natural capital that is essential to ensuring that our environment is resilient in the face of external pressures, such as climate change, and to contributing to human well-being and economic prosperity.

Today, almost 18% of the EU's territory and 4% of its seas are protected as part of the Natura 2000 network,[1] which is at the centre of the EU's nature and biodiversity policy.[2] Yet, Europe's natural capital continues to be degraded and depleted. The EU's target of halting biodiversity loss by 2010 was not reached. Biodiversity loss and ecosystem degradation are also driven by accelerated soil degradation and changes in land use.

The EU Biodiversity Strategy adopted by the European Commission in May 2011[3] commits to halting the loss of biodiversity and the degradation of ecosystem services in the EU by 2020, to restoring them as far as possible, and to strengthening the EU contribution to averting global biodiversity loss. It also sets out a vision for 2050 of protecting, valuing and appropriately restoring the natural capital of the EU. This strategy is in line with the global commitments made in Nagoya in October 2010 in the context of the Convention on Biological Diversity.[4]

Furthermore, in 2006 the Commission adopted a Soil Thematic Strategy and a Soil Framework Directive[5] with the objective of protecting soils across the EU. Land use management lies within the remit of the Member States.

Climate change

Preventing and mitigating climate change is one of the strategic priorities of the EU. The Commission and several Member States are exploring adaptation strategies to strengthen Europe's resilience to the inevitable impacts of climate change.

Over the last 10 years, the EU has significantly reduced its greenhouse gas (GHG) emissions and is well on the way to reaching 20% below 1990 levels as agreed under the Kyoto Protocol.[6] Good progress has also been made towards meeting targets to improve the EU's energy efficiency by 20% and raising energy use from renewable sources to 20%.[7] Europe is working hard to meet its '20-20-20' targets under the climate and energy package by 2020. In order to encourage other nations and regions to reduce their GHG emissions, the EU has offered to step up its cut from 20% to 30% by 2020 if other major economies agree to do their fair share in the global reduction effort.[8]

However, global and European cuts in GHG emissions are far from sufficient to keep average world temperature increases below 2°C. The effects of climate change are already being felt in many European regions. They have implications for human health and well-being, as well as for the health of other species and ecosystems and the services they provide. While some regions will be more seriously affected than others in the short term, all will eventually suffer the effects of this change to varying degrees.

In order to mitigate this, in 2011 the Commission took the first step beyond its short-term climate change objectives for 2020 by presenting a *Roadmap for a Competitive Low-Carbon Economy by 2050*.[9] The roadmap sets milestones for a cost-effective pathway that would result in GHG emissions in the EU being reduced by 80%–95% compared to 1990 levels by 2050. It also provides guidance to those sectors mainly responsible for Europe's emissions, namely power generation, industry, transport, construction and agriculture, on how to make a cost-effective transition to a low-carbon economy. The European Emissions Trading System[10] will continue to play an important role in the implementation of EU climate policy.

Waste

Almost 3 billion tonnes of waste are produced in the EU every year, representing about 6 tonnes of solid waste per person. Ninety million tonnes of this waste is considered to be hazardous.[11] Most of this waste (67%) is disposed of either by incineration or by dumping into landfill. Both methods

cause significant environmental damage. Estimates foresee that by 2020 waste generation will be 45% greater than in 1995. As natural resources become increasingly scarce, Europe has to re-evaluate its management of waste.

In recent years, progress has been made to address the issue of waste and the unsustainable use of natural resources in the EU. In line with the Waste Framework and Landfill Directives,[12] Member States have improved their waste prevention and management efforts. Some have even become global leaders in waste recycling technology. However, sectors and Member States have not implemented the necessary measures to the same degree, and several waste streams continue to grow. On average only 40% of solid waste in the EU is re-used or recycled, with the rest still going to landfill or incineration.[13]

Natural resource management

Competing uses and the legacy of past exploitation have placed natural resources in Europe under severe pressure. The EU needs to produce 'more with less' and to decouple economic growth from resource use, emissions and waste generation. The sectors of nutrition, housing and mobility are responsible for the majority of environmental impacts. Although the EU has succeeded in a relative decoupling of growth and resource use in some areas, a complete decoupling remains challenging, especially in view of largely unsustainable consumption patterns.

The *Roadmap to a Resource Efficient Europe*,[14] which was adopted in September 2011, outlines the structural and technological changes needed to transform the European economy into a sustainable one by 2050, with milestones to be reached by 2020. It proposes solutions that will increase productivity in a resource-efficient manner and decouple economic growth from resource use and its environmental impact.

The Roadmap identifies areas where policy action can make a difference and focuses on overcoming bottlenecks, such as inconsistencies in policy and market failures. Furthermore, it provides a framework within which future actions can be designed and implemented coherently.

Water

Water is vital for human, animal and plant life, as well as an indispensable resource for the economy. It also plays a critical role in the climate regulation cycle. The quantity and quality of water are inextricably linked and have become an increasing cause for concern.

Water quality in the EU has improved under the Water Framework Directive.[15] However, progress has been mixed and several challenges remain. Water stress is becoming a widespread problem in many parts of the EU, particularly in light of climate change. It is important to guarantee supplies, both for human needs and to ensure that ecosystems can deliver their services.

A *Blueprint to Safeguard Europe's Water Resources* was adopted by the Commission in November 2012.[16] The strategy it outlines aims to reinforce water management in order to ensure good quality water in sufficient quantities for all legitimate users. It concentrates on better implementing existing water policies and integrating their objectives into other policies, as well as on filling gaps, in particular with regard to water quantity and efficiency.

The Blueprint is closely linked to the Europe 2020 Strategy and is expected to drive EU water policy up to 2050. The implementation of the Blueprint will be supported by a European Innovation Partnership on Water.[17]

Air quality

Clean air, like water, is essential to our health and the environment. The quality of air in Europe has significantly deteriorated since the Industrial Revolution. Human activities, such as industrial and energy production, and transport, are the main causes of air pollution.

Air pollution in Europe has declined since the early 1970s as a result of EU action to improve air quality, for example by controlling emissions of harmful substances into the atmosphere; improving fuel quality; and

imposing environmental protection requirements on the transport, industry and energy sectors. However, this has not been sufficient to ensure that air quality in urban areas lies within European limits. Exposure to fine particulates and ozone are of particular concern, due to their link to several health issues and reduced life expectancy. It is estimated that, every year, air pollution causes more than 350,000 premature deaths in Europe and costs billions of euros in health expenditure and days of work lost through illness.

In order to address these continuing concerns, a policy process was launched in 2005 under the Thematic Strategy on Air Pollution.[18] Its aim is to make substantial progress towards the long-term EU objective of 'achieving levels of air quality that do not give rise to significant negative impacts on and risks to human health and the environment'.[19]

Chemicals

Chemicals are an important part of our daily life and contribute to the well-being of our society. At the same time, they can also represent a threat to our health and the environment, and be dangerous if not properly used. Man-made chemicals have been found in humans, animals and the most remote environments of the planet, leading to an increasing realisation that the available knowledge base is insufficient for understanding the possible negative effects of chemicals.

The new horizontal chemicals legislation, Registration, Evaluation, Authorisation and Restriction of Chemical Substances (REACH), came into force in the EU in 2007 and has significantly contributed to improving our knowledge of chemicals.[20] However, despite stricter regulation and the phasing out of particularly dangerous substances, EU citizens and the environment are still exposed to multiple pollutants and chemicals, which can lead to long-term damage. Major concerns remain about persistent and bio-accumulative substances, endocrine-disrupting chemicals and heavy metals. There are also significant knowledge gaps in relation to nano-materials and the combination effects of chemicals. Additional legislative work is likely to be required to address these issues.

Sector-based chemical legislation is in the process of being renewed, for example, for the sustainable use of pesticides and the authorisation of plant protection products. A new Regulation concerning the placing on the market and use of biocidal products was adopted in 2012.[21]

Interaction with other EU policy areas

Given the complex and inter-connecting nature of environmental and climate-related challenges, integrating relevant actions into the decisions and activities of other sectors is crucial. Since 1997, it has been a requirement under the Treaty Establishing the European Community that 'environmental protection requirements must be integrated into the definition and implementation of the Community policies . . . in particular with a view to promoting sustainable development'.[22]

The importance of integrating environmental concerns into other policy areas is also reaffirmed in the 6th EAP which states that the 'integration of environmental concerns into other policies must be deepened' in order to move towards sustainable development.[23] The areas for integration include: agriculture and rural development, regional policy, development and cooperation, employment, energy, enterprise and industry, fisheries and maritime affairs, internal market and services, research and innovation, trade, transport, and economic and financial affairs.

The 7th Environmental Action Programme

The proposal for the 7th EAP aims to provide the wide range of existing environmental and climate policies at the EU and Member State levels with a strategic framework that will support their implementation.[24]

A careful analysis of the EU environmental and climate policy under the 6th EAP from 2002 to 2012 has revealed that the programme scored some important successes in driving the environmental agenda, providing a

comprehensive framework for action on climate change and controlling the use of chemicals.[25] However, several unsustainable trends persist in areas such as the preservation of natural capital, the management of natural resources and waste, and climate change, as well as the environment and health, due to failures in implementing relevant policies at the EU, national and regional levels. This is further exacerbated by the new trends and challenges that are arising from demographic changes, urbanisation and technological developments.

The Commission drew upon the lessons from the 6th EAP and a vast quantity of other recent analyses and data when developing the 7th EAP proposal. These include the European Environment Agency's report 'The European Environment—State and Outlook 2010',[26] the OECD's 'Outlook',[27] input from a wide range of stakeholders, a public consultation[28] and an impact assessment for the future programme, as well as official views from other EU institutions.

The resulting programme, to be implemented by 2020, identifies nine priority objectives. The first three are thematic priorities encompassing the different EU environmental and climate policies, priorities four to seven cover broad issues that will support the successful implementation of the thematic priorities, and the last two address challenges specifically related to the urban and global dimensions of the policy.

The three thematic priority objectives

The 7th EAP proposal groups the different environmental and climate change–related challenges highlighted above under three thematic priority objectives where further action is needed—protecting nature and strengthening ecological resilience; boosting competitive, sustainable, resource-efficient, low-carbon growth; and effectively addressing environment-related threats to health and well-being.

Priority objective 1: to protect, conserve and enhance the EU's natural capital

Natural capital is vital for the long-term economic prosperity and well-being of the EU. It encompasses biodiversity and ecosystems and related goods and services, ranging from fertile soil and productive land and seas, to fresh water and clean air. Natural capital also includes services that are often neglected, such as the pollination of plants, natural protection against flooding or fires and the regulation of our climate. Despite a substantial body of legislation, our environment is still under considerable pressure. The loss of biodiversity and the degradation of ecosystems are continuing.

Greater efforts are needed to protect, conserve and enhance the EU's natural capital. The 7th EAP proposal aims to improve the implementation of existing strategies, such as the EU's Biodiversity Strategy and the Blueprint to Safeguard Europe's Water Resources; to review gaps in current legislation in areas such as soil and land use; and to improve existing policies in areas such as forestry. Further action will also be needed to reduce emissions of nitrogen and phosphorus from agriculture and waste water in order to fully comply with air quality legislation and to protect the health of the oceans and seas, whether by increasing the controls on fisheries or by reducing marine litter.

Priority objective 2: to turn the EU into a resource-efficient, green and competitive low-carbon economy

The growth of the EU economy is strongly dependent on the use of fossil fuels and other natural resources. In view of the increasing pressure on natural capital and climate change, it is important to green the EU economy by promoting resource-efficient and low carbon growth. At the same time, the development of environmental technologies and services has already significantly contributed to the competitiveness and growth of European companies in the sector of eco-innovation. Many are world leaders in the areas of recycling and energy efficiency. For example, estimates show that the European renewables sector alone could create more than 400,000 jobs by 2020.[29]

In order to achieve this, the EU has to meet its 20-20-20 climate and energy efficiency goals by 2020 and work towards further reducing GHG emissions by 2050. The environmental performance and resource efficiency of production processes and products (e.g. in the chemical and food industries) need to be improved by applying life-cycle thinking. Furthermore, the overall impact of consumption needs to be reduced. In this context, it is also important to recognise waste as a resource, to encourage more recycling and to phase out landfilling. Targets should also be set for better water efficiency.

Priority objective 3: to safeguard EU citizens from environment-related pressures and risks to health and well-being

Climate change and other environmental issues related, for example, to water, air pollution and chemicals, represent a threat to the health and well-being of EU citizens, and this threat is likely to grow. Already, environmental stressors are estimated to be responsible for up to 20% of deaths in Europe according to the World Health Organization.[30]

Understanding the risks, and properly implementing and adapting existing policy measures, is paramount to addressing these issues, particularly in the areas of air quality, noise, drinking and bathing water, chemicals, and climate change adaptation. The 7th EAP proposal aims to provide a more predictable framework to attract the necessary investment and improve the knowledge base for different environmental threats to health and well-being. It encourages innovation and the development of more sustainable solutions, and calls for existing environmental policies to be updated where appropriate.

A flexible and powerful enabling framework

The new programme provides an enabling framework that will help Europe achieve its environmental and climate change goals. It is based on four 'I's: better *implementation* of legislation, improved *information* for policy design and implementation, more *investment* for environment and climate action, and

full *integration* of environmental and climate-related concerns into other policies. These 'enablers' make up the next four priority objectives.

Priority objective 4: to maximise the benefits of EU environment legislation through better implementation

Improving the implementation of environmental policies will bring many advantages: by ensuring that legislation is put in place in the same way across the EU, stakeholders will be offered a level playing field in the Single Market, innovation will be stimulated through high standards and European companies will be provided with first-mover advantages in many areas of the economy. On the other hand, a failure to properly implement legislation could lead to significant costs, estimated at around €50 billion per year, including those related to infringement cases.

In order to ensure better implementation of EU environmental policies by 2020, the 7th EAP proposal strengthens the implementation agreement between the EU and Member States, and introduces binding criteria for inspections and surveillance activities. It also involves citizens more strongly in the process by putting in place better communication channels at the national level to inform them about how EU environmental legislation is implemented in their Member State and about how to handle complaints regarding this implementation. These proposals will allow better dissemination of information and also improve understanding among citizens of how Member States and regional administrations put EU commitments into effect. In accordance with international treaties, the Lisbon Treaty and recent case law from the European Court of Justice, citizens will be given better access to justice in environmental matters.

Priority objective 5: to improve the evidence base for environment policy

Information is key for the development of good policies and their successful implementation, particularly when addressing complex challenges such as the environment and climate change, which have a strong social and economic dimension. Research, monitoring, indicators and assessments

associated with the implementation of EU environmental legislation contribute to continuously enhancing our understanding of the environment. However, this evidence base needs to be strengthened and updated all the time, and knowledge gaps need to be filled to make sure that policy and business decisions are based on state-of-the-art knowledge about, for example, the risks, costs and benefits of environment and climate policies.

The 7th EAP proposal intends to improve the quality and comparability of data and information on the environment and climate change at the EU and Member State levels by improving their collection, management and sharing. It also supports better coordination of research efforts at these levels to keep the evidence base up to date and to avoid the creation of knowledge gaps. In view of new and emerging issues resulting from technological developments, a more systematic approach to environmental risk management is needed.

Priority objective 6: to secure investment for environment and climate policy and get the prices right

In order to ensure the implementation of the priorities of the 7th EAP proposal and the wide range of environmental issues it covers, more public and private investment will be needed. The economic and financial crisis may discourage some Member States and regions from investing in such activities. At the same time, the structural changes the crisis is engendering also offer new opportunities to move towards more resource-efficient, low-carbon economic models, which will generate significant savings in the long term.

Private investments are often hampered by the absence of clear price signals from the market, price distortions due to the failure to internalise environmental costs or subsidies for activities that harm the environment. In order to ensure that environmental and climate objectives are reached in a cost effective manner and receive the necessary financial support from public and private players, the 7th EAP proposal calls for environmentally harmful subsidies to be gradually lifted, more market-based instruments to be introduced, and the market for environmental goods and services to be

enhanced. To this end, the proposal suggests that a minimum of 20% of the total EU budget from 2014 to 2020 is dedicated to climate mainstreaming in order to ensure a low carbon and climate change–resilient society.[31] Furthermore, it will put in place mechanisms to better track expenditures related to environmental policy at the EU level and to monitor the sustainability of progress.

Priority objective 7: to improve environmental integration and policy coherence

Europe is facing a range of complex and interconnected environmental and climate-related challenges. Addressing these could easily lead to trade-offs being made if their impacts on society and the economy are not carefully assessed. In order to avoid such trade-offs, it is important to further improve the integration of environmental aspects into other policy areas and to adopt a more coherent policy approach. This is likely to lead to solutions that provide multiple benefits to a wider range of stakeholders.

To ensure that by 2020 sector-based policies at the EU and Member State levels support relevant environmental and climate-related priorities, the 7th EAP proposal expects to include relevant conditions and incentives in new and existing policy initiatives. Furthermore, the environmental, social and economic impacts of policies are to be better assessed.

Local, regional and global challenges

The last two priority objectives of the 7th EAP proposal are focused on spatial scales of the EU environment and climate policy, namely on the implications of increasing urbanisation and the global dimension of many environmental and climate-related challenges.

Priority objective 8: to enhance the sustainability of EU cities

Europe is a densely populated region. By 2020, 80% of the EU population is likely to live in or near urban areas.[32] Cities are often confronted

with a common set of environmental problems, such as poor air quality, high levels of noise, GHG emissions, water scarcity and waste removal.

In order to address these issues in an efficient and effective manner, the 7th EAP proposal promotes better coordination between relevant stakeholder groups, and encourages the setting up and expansion of initiatives supporting innovation and best practice in cities, as well as inter-city exchanges and networking. This includes developing criteria to assess cities' environmental performances, taking into account their socio-economic impacts. Furthermore, the financing of urban sustainability needs to be improved. The majority of European cities should be implementing policies for sustainable urban planning and design by 2020.

Priority objective 9: to increase the EU's effectiveness in confronting regional and global environmental and climate challenges

Most of the environmental and climate challenges the EU is facing are interlinked and of a global dimension. Solutions to these challenges can often only be successful if they are part of a global approach or are developed in cooperation with partner countries. This is also necessary to ensure sustainable development at the national, regional and international levels. In particular, the impact of consumption patterns in the EU on third countries must be reduced. 'Living well, within the means of our planet' has to be a truly global aim.[33]

The EU will do its fair share to drive the follow-up progress of the Rio+20 Conference, for example, by working towards adopting Sustainable Development Goals and strengthening the structure of the UN. It will also engage actively in implementing global biodiversity targets under the Convention on Biological Diversity, the United Nations Industrial Development Organization's Chemicals Convention, and other bilateral or multilateral environmental forums.

The 7th EAP proposal commits the EU and its Member States to engaging in processes at the international, regional and bilateral levels in a more

focused, united and coherent manner. This also means strengthening the impact of various sources of funding at the international level, ranging from private investment to development aid.

Conclusion

The 7th EAP proposal is not a Commission work programme, but a strategic overarching framework for the environment for the EU and its Member States. It reflects the EU's commitment to moving towards a smart, sustainable and inclusive economy that secures growth and development, improves human well-being, creates jobs, reduces inequalities, and preserves and invests in its natural capital.

The vision the 7th EAP proposal sets out for 2020 is ambitious but necessary in order to keep the EU on a path to prosperity and health within the limits of the planet. The programme builds on the achievements of the EU's environment and climate policy to date, bringing the overall objectives of these initiatives under one umbrella and showing how they relate both to each other and broader EU objectives. New or updated targets will only be introduced where policy gaps are identified and action is needed.

Shortcomings in the implementation of the current EU environmental and climate policy are addressed by providing a more integrated and enabling policy framework that formulates 'what needs to be done and how'. Environmental and climate actions are far more integrated in the programme, and better coherence and integration in other policy areas are also provided for, in order to avoid potential conflicts or trade-offs. Furthermore, existing regulatory instruments, such as subsidies, are to be reviewed. The proposal also ensures that regional and global aspects are better taken into account.

Although the proposal for the 7th EAP that was adopted by the European Commission in November 2012 was developed in consultation

with the different EU institutions, it will need to obtain the official backing of the Council of the European Union and the European Parliament. Once it has been finally agreed by all three institutions, it will become the guiding policy for environmental and climate-related issues until the end of the decade.

In the end, the success of the 7th EAP will depend on the actions of the EU and its Member States.

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Agricultural and Rural Policy

Introduction

Why do we still have a Common Agricultural Policy?

The Common Agricultural Policy (CAP) is one of oldest policy areas in the EU; from the very beginning it was an important bond in the European Community. Right from the start, the Common Market was intended to include both trade and industry, and agriculture. Just as agriculture in the EU has been modernised over the past 50 years, so too has the CAP. As a result of a series of reforms—notably the 1992 McSharry reform and the Fischler reform in 2003—the CAP has changed significantly in order to adapt to the current needs of land use and food production as well as the needs of society at large.

Agriculture will continue to be a central pillar of the EU, both due to the importance of providing food for over 500 million EU citizens and its shear land coverage. At present, 80% of the EU land mass is arable. A policy covering this area remains important for the EU and its Member States. EU citizens expect the European landscape to be preserved and nurtured.

The recent sensitive political decisions in the field of energy supply and food supply show how important it is for the EU, just as for states, not to ignore the need to have a secure food supply for its population. Moreover, the productive capacity of its food industry must be supplied with raw materials that it has grown itself. Consumers want high-quality food products which adhere to EU standards and are reasonably priced. This requires a sustainable and efficient agricultural sector in the EU. At the same time, agricultural policy must take new challenges into account, such as climate change and the sensitive question of the use of genetic technologies.

As the only fully EU-wide common policy, the CAP serves a single common European agricultural market, financed entirely via the EU budget on

a Community level (i.e. under the first pillar, in other words through direct payments and market expenditure), which means that countries refrain from national subsidies. This fact is too often forgotten by those who criticise the high proportion of agricultural subsidies in the EU budget. In fact, agricultural subsidies have already declined from 0.61% of the EU GDP in 1993 (EU12) to 0.43% by 2004 (EU25) and shrank even further to 0.30% in 2013.

The objectives of EU agricultural policy

The objectives of the CAP, formulated in Article 33 of the Treaty Establishing the European Community, are the following: to increase the productivity of agriculture, especially per unit of labour; to secure an appropriate level of income for the rural population; to stabilise the markets; and to ensure a reliable food supply at prices consumers can afford.

The Treaty of Lisbon, Article 39 has not changed these objectives, although as a result of the Fischler reform of 2003, the objectives have been widened to correspond to reality. An additional focus of the CAP on the environmentally sustainable use of land has also been formulated, which was intended to make an active contribution to the preservation of the landscape, nature and the environment. The formal confirmation of the second pillar of the CAP, the policy for the development of rural areas, meant that the strengthening and preservation of the overall functionality of rural areas became one of the major objectives of the CAP.

The essential instruments of agricultural policy

In order to realise the objectives of the CAP, the Community created three fundamental instruments:

1. *Community preference*. This was intended to protect European products in many different agricultural sectors from (cheaper) imports from third countries, thus giving European products an advantage in the internal market.

2. *Direct payments*. These are product-unrelated payments that are only made when certain obligations have been fulfilled.

3. *Shared financing.* The costs of implementing the CAP are financed from the EU budget, specifically from two funds that are part of the total budget of the EU:

   - The European Agricultural Guarantee Fund (EAGF) finances both direct payments to farmers and other market expenditures, such as intervention measures and export rebates.

   - The European Agricultural Fund for Rural Development (EAFRD), previously the European Agricultural Guidance and Guarantee Fund,[1] funds the programmes of the Member States for rural development. These programmes have to be co-financed out of the national and regional budgets.

Both funds were established by Council Regulation (EC) no. 1290/2005 of 21 June 2005 on the financing of the CAP.[2] The maximum amount of funds to be appropriated for the period 2007–13 for the CAP is €421.1 billion, of which €336.6 billion has been earmarked for direct payments and market expenditures and €91.3 billion is allocated to EAFRD expenditures.

Out of respect for European taxpayers, it is important to ensure that these funds be allocated appropriately. To do so, management systems and controls have been established that offer the appropriate checks to make sure that the funds are allocated properly and to ensure that payments contrary to the regulations are discovered and returned to the fund. According to the ground rules for the financial administration of the CAP, the Commission is responsible for the management of both funds. The Commission itself, however, gives no money directly to the final recipients (for example, individual farmers). In line with the principle of shared intermediate management, this is the responsibility of the Member States that have mandated national or regional payments agencies to allocate the

funds. Before these payments agencies can apply for reimbursement from the EU budget, they have to meet the criteria laid down by the Commission for such agencies and be accredited. However, the payments agencies are not only responsible for payments to the beneficiaries but before making any payments they must be satisfied, or have ascertained that the responsible agency is satisfied, that the application for aid was eligible.

A key element in the discussion concerning the arrangement of the financial framework is the debate between the net contributors, especially Germany, the Netherlands, the UK and Sweden, and the recipient countries. The debate on redistribution among the 27 Member States within the context of the CAP arose during discussions concerning Health Checks (see below) and remained vigorous in the discussions on the CAP post-2013 budgetary envelope.

The McSharry reform, 1992

The need for reform

The first two decades of the CAP resulted in enormous surpluses in some areas. This was due to the policy failure of the market regime to adapt; because of the food shortages following the Second World War, it had focussed on increasing production. Since 1984, the EU has made a number of attempts at reform (e.g. milk quotas stabilisers and price discipline) in order to address this problem. In the Uruguay Round (of the GATT world trade talks),[3] which began in 1985, agricultural products were included for the first time in an attempt to liberalise global trade. To begin with the Community blocked all initiatives to liberalise trade in agricultural products, and the round almost ended in failure. In order to pave the way for a final agreement, the Community agreed in 1992, under great pressure, to reform the CAP. The McSharry reform was agreed to overcome two major obstacles: a mounting budget for supporting agricultural production and the inclusion of agriculture in the trade talks.

Essential elements of the agricultural reform of 1992

Market reforms

The agricultural reforms of 1992 set in motion a reform process which continues and which has fundamentally altered the structure of the CAP. Direct income supplements were incorporated into the market regulations in the form of compensation for the reduction of price supports. In general, this aid was based on the number of animals or the area of land ('Blue Box measures' in World Trade Organization (WTO) terminology).[4] These supplements could be dependent on the amount of land, level of income or level of employment, or even be allocated regionally. As long as there were reductions in volume (via quotas, idling of production, intensification of production, etc.), the results could be compared using similar criteria. In this way it was possible at the same time to create a price policy that improved the competitiveness of European agriculture, stimulated consumption and permitted agricultural products to be used for purposes other than food. The basic principle of the reform was that production was decoupled from the support given. The principle of decoupling was introduced with the 1992 reform. A 15% mandatory set-aside was introduced to combat overproduction.

Accompanying measures

Within the framework of the 1992 reforms, flanking or accompanying measures were also introduced. These are independent of production and therefore qualify as Green Box measures, according to WTO terminology.[5] This exempts them from the WTO obligations to reduce subsidies. The measures in question deal with environmental protection (Council Regulation (EEC) no. 2078/92),[6] the regulation of early retirement (Council Regulation (EEC) no. 2079/92)[7] and reforestation measures (Council Regulation (EEC) no. 2080/92).[8]

The Fischler reforms since 1999

Agenda 2000

The goals of the Agenda for agriculture

At the European Council meeting of 26 March 1999 in Berlin, the heads of state and government came to a political agreement on Agenda 2000 and affirmed the objectives adopted for agricultural policy. A deepening of the 1992 reforms was attempted, so that the CAP would be ready for the challenges of the EU's imminent eastern expansion and the increasing globalisation of agricultural trade after 2000.[9] The new proposals for reform were, therefore, intended to secure European agriculture and life in rural areas under modern conditions. This first required acknowledging that today's farmers have to combine the production of high-value agricultural goods with the protection of the environment by taking care of the landscape and natural habitat (multifunctionality).

Protection of the environment requires, however, that the role of farmers in taking care of nature be recognised and that their efforts to do this be compensated with direct payments, although the agricultural lobby claims that this is compensation for compensation. This would make it worthwhile for farmers to produce less intensively and to use production methods and inputs that are better for the environment. In addition, the production of raw materials for the non-food sector (renewable resources) will become more important. Rural development depends in any case less and less on the agricultural sector. Other new forms of economic activity must contribute to keeping the population in rural areas and to strengthening its economic capacity. Support such as that of the new second pillar of the CAP in favour of rural areas should therefore be increased (see below).

Moreover, it must be borne in mind that the EU supports international trade rules (i.e. the GATT and the WTO) and is aware of its responsibility

as the largest importer and exporter of agricultural goods in the world. The food industry in Europe (measured by value of goods produced) is the largest industrial sector (measured by revenue). Furthermore, the EU has ratified a number of trade agreements (with the Mediterranean neighbourhood and South Africa) or is actively seeking to do so (with Mercosur, Mexico, the ACP group of states),[10] which should lead to free trade zones where trade in agricultural products will be governed, almost without exception (*de minimis* rules would apply), by the general rules of the Marrakesh Agreement. The goal, in other words, is to be well prepared for the next WTO round. Until now there has been no final agreement on the WTO rounds. It is difficult to predict the result of negotiations still underway and how any final result will affect the future development of the CAP. Nevertheless, international discussions played an important role in every stage of reforming the CAP. Among the significant elements of Agenda 2000 are the reform of the market organisations, the introduction of the second pillar for rural development and the option of making direct payments conditional.

Reforming the market organisations

Reforming the market organisations changed the current system, especially in the areas of grain, beef and milk. In the case of grain and starch potatoes, support purchases were reduced and a single arable crop premium was introduced. Initially, the guideline for fallow land was set at 10% of arable land. As of 2002–3, the amount paid per area for grain was also applied to vegetable oil. The price intervention for beef was adjusted in three stages to 20% and replaced with private storage. A security net was maintained. The extensification premiums were raised, although an additional slaughter premium was added, to be introduced in stages. This was at Germany's request and includes milk cows and calves. At France's urging, the heads of state and government modified the agreement of the agriculture ministers to postpone reforms to the market for milk by two years, until 2005–6. As a result, the agriculture ministers kept the quota regulations in force until 2008. Also, the re-examination of the quota regulations in 2003 was confirmed.

The second pillar: rural development

One central focus of rural development is strengthening the agricultural and forestry sectors through various measures: encouraging young farmers, implementing pre-retirement regulations, educating and further training farmers, and modernising agricultural industries, as well as promoting the processing and marketing of agricultural products. In the context of programmes to promote investment, which could include part-time farmers, important factors are the reduction of production costs and the improvement of product quality, as well as environmental, health and animal protection measures and the promotion of diversification of income.

A second central focus of the basic regulation is improving the competitiveness of rural areas. Measures in this area are intended to support the quality of life in rural areas and a diversification of economic activities. Agricultural measures are important here; for example, advising, marketing high-quality products, soil improvement, land rotation, village renewal and development, improvements to infrastructure that are important to agriculture, measures in favour of environmental and animal protection, and measures to protect the landscape from natural disasters.

Finally, a third central focus of the policy for rural areas is the protection of the environment and action to protect the natural heritage. In addition to pre-existing measures for the protection of the agricultural environment, equalisation support for less-favoured areas (LFAs) was included, because they are ecologically sensitive. Similarly, the strengthening of non-food production and ecological enhancement need to be promoted in those areas in the context of rural development.

Making direct payments conditional

The possibility of cuts to direct payments was kept open by the Commission, both within the framework of Agenda 2000 and in the context of the Health Check; this caused intense debate and remains a topic for discussion for the post-2013 CAP. Since 2000, direct payments have been

tied to fulfilling certain environmental conditions that go beyond those recommended by good agricultural practice. In addition, the Commission kept the right, enacted by the Member States, to reduce the direct payments by up to 20% (modulation), provided they take into consideration the amount of activity, the economic situation of the businesses and the total value of the payments granted during a calendar year.[11] The monies saved are kept by the Member States and can be used for additional policy measures that promote rural areas, including co-financing.

Reform following the mid-term review

Analysis of Agenda 2000 decisions

The most important part of Agenda 2000 was a deal between then German Chancellor Gerhard Schröder and former French President Jacques Chirac, whereby the CAP budget was fixed until the end of 2013. This agreement overshadowed the entire reform. But, by the end of the 1999 Berlin summit, it had already become clear that new reforms would be necessary in 2002–3, especially in those sectors that were not subject to reform (sugar and wine) or had not been immediately reformed within the framework of Agenda 2000, such as milk, as notable overproduction was continuing and could be brought into equilibrium only by means of export supports and other measures (drastic reforms). For this reason, a mid-term review was agreed upon. The 2003 reform also introduced the single farm payment (SFP), merging headage payment and acreage payment into one payment.

Decoupling. This principle, that payments are no longer tied to the volume of a particular product (see above), was introduced with the McSharry reform and fully implemented from 1996.The Community wanted to move away from an orientation on production geared towards optimising premiums, towards a market orientation. The 2003 reform also sought to decouple payments from historical performance and to put in place the 'regional payment' scheme. However, as there was no clear majority for it, the introduction of the regional payment scheme was implemented on a voluntary basis, which resulted in the situation depicted in Table 1.

Decoupling began in a thorough way on 1 January 2005; thereafter, support was given on the basis of the average payments of 2000–2. The Member States had various options for calculating and implementing direct payments. Essentially, it is necessary to decide whether the operating premium is determined on the basis of the overall production of individual farmers in the relevant period (2000–2), or if the average of all the combined historical payments made to the farmers is used as a basis for paying support. This average is then paid throughout the region or the entire state; in doing so, a distinction can be made between pasture and cultivated land. In this way it is possible to distinguish between a historical model of organisation and regional models (static or dynamic) although a mixed model is also possible. Today, about 90% of the direct payments are decoupled but only on the farm basis and not on the area.

Table 1 The payment schemes selected by the EU15 countries

Historical model	Hybrid model	
	Static	Dynamic
Austria, Belgium, France, Greece, Ireland, Italy, Netherlands, Portugal, Spain, UK (Scotland and Wales)	Denmark, Luxembourg, Sweden, UK (Northern Ireland)	Finland, Germany, UK (England)

The diverging 'phasing-in' system for the new Member States, to which they apply the single area payment scheme (SAPS), is quite similar to a decoupling unified hectare system within a regional model.

Nevertheless, countless exceptions remained that made it possible to continue with coupled payments, notably through Article 68 (formerly Article 69).[12] For farmers and agencies this means the parallel administration of two payment and control systems. In the case of cultivated land, for example, up to 15% of the direct payments could

remain coupled. In the case of the animal premium, direct payments for sheep and goats, which are typical areas of production in underdeveloped areas, can be coupled to 50% in order to prevent farming being abandoned in these sensitive areas. The same is true of the beef premium, for which payments can remain coupled up to 100%. For the first time, premiums were allowed to be given for pasture and could reach the same level as those for cultivated land. In the case of milk, the decoupling of direct payments will be undertaken after the reforms already introduced have been concluded. Nevertheless, Member States that take advantage of the possibility to grant premiums for pasture can decouple milk premiums (as Germany has done).

The discussion about the ‘better’ model arises again and again. Today it is clear that every adjustment to the system becomes an administrative burden, for farmers as well as for administrators, but—usually after a certain learning curve—the advantages of simplification eventually become visible.

Cross-compliance and the farm advisory system. A necessary precondition for the full grant of the decoupled direct payments is compliance with selected regulations in the areas of environment and animal protection, as well as food safety ('cross-compliance'). The regulation is the result of two fundamental goals:

- to contribute to more sustainability in agriculture, and
- to bring the CAP better into harmony with the expectations of consumers and taxpayers.

The regulation anticipates that the direct payments to the farmer can be reduced or suspended if certain requirements are not fulfilled. There are essentially two main areas of requirements: the ‘statutory management requirements’ and ‘good agricultural and ecological condition’. The statutory management requirements originally comprised 19 regulations. The Member States must establish minimum standards on the basis of EU law for what constitutes good agricultural and ecological conditions. The applicable

regulations deal with key elements, such as the environment; animal tagging; the health of humans, animals and plants; and the protection of animals.

Modulation. In 2005, a single fund for the second pillar of the CAP, the EAFRD, was agreed, bringing together all previous measures. Because the overall budget for the CAP had been fixed until 2013, it was necessary to make more money available for rural development. Modulation of direct payments was therefore made obligatory on 1 January 2007. This means that a certain percentage of the direct payments are redirected to the second pillar. In the reallocation of the modulation amounts, it is anticipated that at least 80% of the money will remain in the Member State to which it has been directed. The rest, to a maximum of 20%, will be paid out to the Member States according to a schema proposed by the Commission. Modulation is not applied to farmers who receive less than €5,000 in direct payments or to those in the 'outermost regions'. In the new Member States, modulation will be applied only when they have achieved parity of support at the level of the EU15.[13] In addition, a voluntary modulation of a further 19% was granted to Portugal and the UK. For Portugal, the voluntary modulation was exempt from co-financing.

New budget mechanism. It was decided that, in order to protect budgetary discipline in the face of the imminent breaching of the safety margin (€300 million below the upper limit), the Commission would present a proposal no later than 31 March in a year affected by the required reduction in direct payments and that the Council would make a decision no later than 30 June. If reductions are in fact agreed upon, farmers who receive less than €5,000 per year in direct payments would be exempt. Similarly, the new Member States would be exempt, as long as they have not reached the general level of direct payments in the EU15.

Strengthening rural areas. In order to promote the development of rural areas, many new programmes are being created. Among them are the development of young farmers, investment assistance for processing plants, and programmes to promote improvements in animal protection and the quality of food products. In addition, measures to raise the standards of production and increase cooperation among growers are to be promoted. In

the proposals for new financial projections, three primary goals and one new concept for LEADER (links between actions of rural development) have been formulated.[14] The three primary goals are improving the competitiveness of agriculture and forestry; improving the environment, landscape and the quality of life in rural areas; and promoting the diversification of the rural economy. In addition, a new concept for LEADER was created, whereby local development strategies are carried out by local action groups.

Changes to the market organisation. Whereas decoupling and modulation had only a limited influence on agricultural trade in the EU, the changes to the organisation of agricultural markets were of fundamentally greater importance. The consequences in the area of land cultivation remained limited, since the intervention price for grain remained unchanged and was not reduced by an additional 5% from that in Agenda 2000, as per the proposal retabled by the EU Commission. In the economic year 2004–5, the intervention price remained at €101.31 per ton. The basic amount for calculating the direct payment remained unchanged at €63 per ton.

In the dairy sector, the reduction in intervention prices for butter and skimmed milk powder was in fact greater than had been agreed to in Agenda 2000 but remained considerably below that proposed by the Commission. The intervention price for butter was reduced in four stages by 25%. The skimmed milk price was reduced in three stages of 5% each in 2004, 2005 and 2006. The different rate of reduction was contested from the beginning in an attempt to bring the growing production of butterfat under control. The price reductions in excess of those proposed in Agenda 2000 were set at an average of 80%, which was well above the level of 58% anticipated in Agenda 2000. The increase in milk quotas agreed upon in Agenda 2000 was postponed until 2006–7. By that time there were already clear signs of a political majority in favour of letting the quota system expire.

Special crops. Aid was reduced for many special crops, such as durum wheat, or was changed into product-specific, linked direct payments, for protein crops, for example. Direct aid for potato starch was kept at the level of €11.54 per ton of starch. Otherwise, the processing aid for starch

remained the same as for dried fodder. To raise energy crops, aid of €45 per hectare was introduced for a maximum area of 1.5 million hectares, although there had to be a cultivation contract between farmer and processor. Over time this instrument was discovered to be impracticable, so it was abolished in the Health Check. The Council agreed on a 50% delinking for all tobacco producers, beginning in 2010. This allowed for sufficient incentives to be created to match European production to demand while ending the contradiction that the EU was both promoting the production of tobacco and combating tobacco consumption. In the case of hop production the Council decided in April 2000 on a proposal to move to a premium per hectare as recommended by the Commission.

Reforms under Commissioner Mariann Fischer Boel

The Health Check

In the era of Commissioner Fischer Boel, the Health Check was the greatest challenge. The agriculture ministers of the EU reached agreement on the issue on 20 November 2008. This was not a case of a further reform but rather of conforming to the decisions agreed upon in 2003 and their further development. Among the most important measures are the continued decoupling of support payments, the abolition of set-aside, the confirmation of abolishing milk quotas in 2015 and the transformation of market interventions into a security net. Beyond this, modulation will be was increased; that is, the direct payments to farmers will be reduced and the money freed up and thereby transferred to the second pillar. Out of this fund the Member States can finance measures to meet ‘new challenges’ as defined in the framework of the Health Check. Among these are combating climate change, water management, the protection of biological diversity and the development of bioenergy. Moreover, Germany succeeded in having the restructuring of the dairy sector added to this list as a new challenge, so that the specially designated money could also be used in this sector. Because of the change to the programme for rural development, most

Member States have decided to use the largest portion of the funds freed up for measures to promote biodiversity and water management.

In light of the expiration of the milk quota regulation in 2015, the agriculture ministers decided to increase the quota by 1% annually from 2009 to 2014. The intention is to make it possible for the sector to prepare for the expiration of the quota and ensure that there will be a soft landing, since prices will drop sharply in 2015. Italy was permitted to frontload its quota by 5% in one step in 2009–10. The Council thereby demonstrated a clear political will with a large majority to exit from the quota regulation.

The decision to decouple direct support was extended further in that the coupled payments were incorporated into the system of a single payment per farm. Only a few exceptions remain, the last bastion of the historical agricultural policy: the suckler cow premium and the premium for sheep and goat meat can be retained in 'linked' form at current levels. In the Council, Germany, for example, has made it clear on more than one occasion that it intends to implement full decoupling by 2013, including in this area.

To give Member States the flexibility to support sectors with special challenges, to support measures for environmental protection or to improve the quality and marketing of agricultural products, Member States were permitted to withhold 10% of the national limit on direct payments to each sector and allocate this to a specific sector (the Article 68 measures of Council Regulation (EC) no. 73/2009).[15] Other possible ways of intervening include measures in the area of risk management (included at the request of France and Spain), regulations for crop insurance in case of a natural disaster or reciprocal funds in the event of the outbreak of an animal disease. The Member States that apply the single payment regulation cannot at present use the funds allocated to them under their national framework for Article 68 measures, nor can they transfer this money to the fund for the development of rural areas.

The proposal by the Commission to increase the modulation was contentious. The Member States were able to agree that direct payments

greater than €5,000 could be reduced annually until 2012 by a total of 10%. The amount saved will be added to the budget for the development of rural areas. A reduction in direct payments for large farms was discussed once again, with opposition from Germany and the UK. Because of the active intervention of these two countries, but also because of the support of the European Parliament for their position, this proposal was defeated. The new 'modulation solution' was the compromise that was achieved. For payments greater than €300,000 per year, an additional deduction of 4% will be considered. The funds gained from the reduction in direct payments can be used by the Member States for the 'new challenges'. The EU co-finances up to 75% of the transferred amounts and up to 90% in the convergence regions with a low average gross domestic product.

The requirements for cross-compliance were further simplified and improved (see below); that is, certain standards that are not relevant, or for which the farmer is not responsible, were deleted. At the same time there will be new requirements to preserve the natural state of the areas set aside and to improve water management. Certain standards will be optional under specified conditions.

As a result of the Health Check, the intervention for pork was abolished and was reduced to zero for malted barley and sorghum. There were new conditions for intervention purchases of bread wheat, butter and skimmed milk powder; these will be purchased by tender up to the amount by which the upper quantity is exceeded. Also delinked were small support regulations, which were incorporated into the single payment scheme in 2012. The premium for energy crops was abolished as well.

The sugar market

In 2006, the common market organisation for sugar was reworked, and the entire sector was thoroughly reformed.

Key elements of the reform are the reduction in the guaranteed minimum price for sugar, compensation payments to farmers and a restructuring fund

to encourage sugar producers who are uncompetitive to withdraw from production. A time-limited restructuring fund was brought in (under pressure from the sugar industry) to support the restructuring process. The common organisation for the market for sugar anticipates further interventions in the internal market, among them, establishing a reference price and production quotas, as well as support measures for European products marketed globally. The goal was to reduce the quota by approximately six million tonnes in order to reach market equilibrium following the four-year transition period. When a production facility is shut down completely, compensation is paid per ton of quota surrendered from the restructuring fund. The compensation is reduced annually. The decisive factors provoking the reforms were the high price of sugar in the EU relative to prices on the international market and the fact that the export system was contrary to international trade rules. Therefore, the EU decided that, beginning in 2009, its market would be completely open to imports from the 49 poorest countries in the world. Exports from the EU declined dramatically, thereby enabling the EU to fulfil its WTO obligations.

Reform of the wine sector

Also drastic was the reform agreed to in December 2007 of the common organisation of the market for wine. This reform anticipates a restructuring of the wine sector in order to increase the competitiveness of European wine producers. Every year, 175 million hectolitres of wine are produced in the EU, which has 45% of the world's vineyards. Key elements of the reform include, among other things, a voluntary three-year grubbing-up period (up to 175,000 hectares), the creation of national financial frameworks, the abolition of the right to plant by the end of 2015 (on the Member State level by 2018), preservation of chaptalisation[16] (this was important to the Nordic wine-producing countries), the phasing-out of crisis distillation, the protection of certain forms of bottling (for example, the Bocksbeutel) and the regulation of quality wine.

In the context of national financial frameworks, the Member States can support their vintners through appropriate measures, for example, the promotion of exports to non-EU countries, the restructuring of vineyards or

changing crops, investments for modernisation, support for green harvesting, and new measures for crisis management, as well as simply giving support independently of production.[17] Financial resources that have been allocated to the sector for measures to improve the land will be handed over. These will support additional measures: assistance for young vintners to get established, improved marketing, career training, promotion of grower organisations and so on. The subsidies for crisis distillation used in the southern Member States will be phased out over four years, ending in the fiscal year 2011–2, and those for the distillation of drinking alcohol will be abolished within four years.

Reform of the fruit and vegetable sectors

Since 1 January 2008, there has also been a new common organisation of the market for fruit and vegetables, which is intended to improve the competitiveness of this sector as well. The goals are to improve the market orientation of the fruit and vegetable sector, to smooth out the swings in income caused by crises, to promote exports, and to improve environmental protection. The reform strengthens the position of the producer organisations, which more fruit and vegetable farmers are encouraged to join. The producer organisations will be given tools for crisis management, and up to 50% of the costs will be funded by the Community. In addition, support payments for processed fruit and vegetables will be delinked from the amount produced and handed over to the national authorities responsible for the single payment scheme. This amounts to a transfer of €800 million. A new feature is that, with the inclusion of fruit and vegetable production in the single payment scheme, the cross-compliance regulation will become compulsory. In addition, the producer organisations must use at least 10% of the funds of every operational programme for measures to protect the environment. In all operational programmes, organic farming is 60% co-financed by the EU.

Simplification of the CAP

The reduction in the amount of regulation and the abolition of unnecessary bureaucracy is an ongoing task for the EU. In the context of the

CAP, in 2005 the Commission proposed a comprehensive simplification. Building on the improvements that were implemented in the reforms described above, numerous laws pertaining to the various agricultural sectors were harmonised and brought together. In 2007 it was also decided to create a unified common market organisation, replacing the 21 existing common market organisations.

The regulations regarding cross-compliance are often criticised as too bureaucratic. In a 2007 report on cross-compliance, the Commission implemented a series of measures to improve and simplify the cross-compliance regulations. The objectives of these changes are, among others, better information, a degree of tolerance towards minor violations, the harmonisation of controls and the introduction of advance notice in the case of certain farm inspections.

Commission proposals for the CAP after 2013

The Commission Communication of 2010

In its 2010 Communication, *The Common Agricultural Policy (CAP) Towards 2020: Meeting the Food, Natural Resources and Territorial Challenges of the Future*, the Commission aimed to make the European agriculture sector more dynamic, competitive and effective in responding to the Europe 2020 vision of stimulating sustainable, smart and inclusive growth.[18] Earlier that year, the Commission held a public debate and a major conference on the future of the CAP. The vast majority of contributions identified three principal objectives of the CAP:[19]

- *Viable food production*. This refers to the provision of safe and sufficient food supplies in the context of growing global demand, economic crisis and much greater market volatility, in order to contribute to food security.

- *Sustainable management of natural resources and climate action*. Farmers often have to put environmental considerations ahead of economic ones, but such costs are not rewarded by the market.

- *Maintaining the territorial balance and diversity of rural areas*. Agriculture remains a major economic and social driving force in rural areas and an important factor in maintaining a living countryside.

The Communication therefore looked at the future instruments that might be suitable for best achieving these objectives. For *direct payments*, the Communication outlined the importance of a redistribution, redesign and better targeting of the support, based on objective and equitable criteria, easy to understand by the taxpayer. These criteria should be both economic (noting the 'income support' element of direct payments) and environmental (reflecting the public good provided by farmers), and the support better targeted towards active farmers. A more equitable distribution of funds should be organised in an economically and politically feasible way, with a transition to avoid major disruption.

One approach could be to provide a basic income support payment (which might be uniform per region but not flat-rate across the EU, based on new criteria and capped at a certain level); plus a compulsory environmental payment for additional actions (annually) which go beyond the basic cross-compliance rules (such as green cover, crop rotation, permanent pasture or ecological set-aside); plus a payment for specific natural constraints (defined at EU level) and complementing amounts paid via Rural Development measures; plus a limited 'coupled' payment option for particularly sensitive types of farming (similar to the current option introduced (under Article 68) in the CAP Health Check). A simple, specific support scheme should enhance the competitiveness of small farms, cut the red tape and contribute to the vitality of rural areas.[20]

On *market measures*, such as public intervention and private storage aid, there may be some scope for streamlining and simplifying, and possibly

introducing new elements with regard to improving the functioning of the food chain. Although these mechanisms were the traditional tools of the CAP, subsequent reforms have enhanced the market orientation of EU agriculture and reduced these to safety net measures, to the extent that public stocks have virtually been eliminated. Whereas market measures accounted for 92% of CAP spending as recently as 1991, just 7% of the CAP budget was spent on them in 2009.

Rural Development policy has allowed the economic, environmental and social sustainability of the farming sector and rural areas to be enhanced, but there are strong calls to fully integrate environmental, climate change and innovation considerations into all programmes in a horizontal way. Attention is drawn to the importance of direct sales and local markets, and the specific needs of young farmers and new entrants. The LEADER approach will be further integrated. In order to be more effective, a move towards a more outcome-based approach has been floated, perhaps with quantified targets. One new element in future rural development policy should be a *risk management toolkit* to help deal better with market uncertainties and income volatility. Options should be open to Member States to address production and income risks, ranging from a new WTO-compatible income stabilisation tool, via strengthened support, to insurance instruments and mutual funds. As with direct payments, there should be a new allocation of the funds based on objective criteria, while limiting significant disruption from the current system.

The Communication outlined three options for the future direction of the CAP, in order to address these major challenges:[21]

1. adjusting the most pressing shortcomings in the CAP through gradual changes;

2. making the CAP greener, fairer, more efficient and more effective; and

3. moving away from income support and market measures, to focus on environmental and climate change objectives.

In all three options, the Commission provided for the maintenance of the current system of two pillars: the first pillar covers direct payments and market measures, whereby rules are clearly defined at EU level; and the second pillar comprises multi-annual rural development measures, whereby the framework of options is set at EU level, but the final choice of schemes is left to Member States or regions under joint management. Another element common to all three options is the idea that the future system of direct payments cannot be based on historical reference periods but should be linked to objective criteria. 'The current system provides different rules for the EU 15 and the EU 12, which cannot be continued after 2013', as Commissioner for Agriculture and Rural Development Dacian Cioloş stated.[22] More objective criteria are also needed for rural development allocations.

Commission proposals of 2011

The Commission's blueprint to reform the CAP after 2013 aims to strengthen the competitiveness and the sustainability of agriculture and maintain its presence in all regions, in order to guarantee European citizens healthy and quality food production, to preserve the environment and to help develop rural areas. In the press release, Commissioner Cioloş said:

> The European Commission has proposed a new partnership between European citizens and its farmers to meet the challenges of food security, sustainable use of natural resources and growth. The coming decades will be crucial in laying the foundations for a strong agriculture, able to deal with climate change and international competition, while meeting public expectations. Europe needs its farmers. And its farmers need the support of Europe. The Common Agricultural Policy is our food production, and is the future of over half of our territories.[23]

In addition, he stressed that, in line with the other Commission policy initiatives for the period after 2013, the reformed CAP will make a decisive contribution to Europe 2020. It will fight against climate change, support

employment and growth, promote innovation, and enhance both the economic and ecological competitiveness of agriculture.

The 10 key points of the reform are:[24]

1 Better targeted income support to stimulate growth and employment:[25] To better develop the agricultural potential of the EU, the Commission is proposing to support farmers' income in a fairer, better targeted and simpler way. Basic income support will only cover active farmers. It will be degressive from €150,000 per holding and capped beyond €300,000, taking into account the number of jobs created. It will also be distributed more equitably among farmers, among regions and among Member States.

2. Crisis management tools that are more responsive and better suited to meeting new economic challenges:[26] Price volatility is a threat to the long-term competitiveness of the agricultural sector. The Commission is proposing safety nets (intervention and private storage) which are more effective and more responsive for the sectors most exposed, and the promotion of the creation of insurance and mutual funds.

3 A 'green' payment for preserving long-term productivity and ecosystems:[27] To strengthen the environmental sustainability of agriculture and enhance the efforts of farmers, the Commission is proposing to spend 30% of direct payments specifically on the improved use of natural resources. These measures—crop diversification, maintenance of permanent pasture, the preservation of environmental reservoirs and landscapes—are practical and simple to implement and will have a genuine ecological effect.

4 Additional investment in research and innovation:[28] To produce more, with less, and better, the Commission is proposing to double

the budget for agricultural research and innovation, including through a new European Innovation Partnership. These funds will support research projects relevant to farmers, encourage closer cooperation between scientists and farmers and the quicker transfer of positive results from the laboratory to the field, and provide better information and advice to farmers.

5 A more competitive and balanced food chain:[29] Agriculture plays a vital role as the first step in the food supply chain, but the sector is highly fragmented and unstructured, and its added value is not recognised. To strengthen the position of farmers, the Commission is proposing to support producer organisations, develop inter-professional organisations, and develop direct sales between producers and consumers. Sugar quotas, which have lost their relevance, will not be extended beyond 2015.

6 Encouragement of agri-environmental initiatives:[30] The specificities of each territory should be taken into account, and environmental initiatives will be encouraged at national, regional and local levels. For this, the Commission is proposing two specific Rural Development policy priorities for restoring, preserving and enhancing ecosystems and for resource efficiency and the fight against climate change.

7 Facilitation of the establishment of young farmers:[31] Two-thirds of farmers are over 55. To help the younger generation to get involved in the agricultural sector, the Commission is proposing to create a new installation aid available to farmers under 40 years old, during the first 5 years of their project.

8 Stimulation of rural employment and entrepreneurship:[32] To promote employment and entrepreneurship, the Commission is proposing a series of measures to stimulate economic activity in rural areas and encourage local development initiatives. For example, a ‘starter kit’ will be created to support micro-enterprise projects with funding of

up to €70,000 over 5 years. The LEADER local action groups will be strengthened.

9 Better addressing of fragile areas:[33] To prevent desertification and preserve the richness of our land, the Commission is providing an opportunity for Member States to give additional support to farmers in areas with natural disadvantages. This is in addition to other aid already available under the rural development policy.

10 A simpler and more efficient CAP:[34] To avoid unnecessary administrative burdens, the Commission is proposing to simplify several of the administrative mechanisms of the CAP, such as the rules of conditionality and control systems, without losing efficiency. Moreover, aid to small farmers will be simplified. For the latter, a flat rate of €500–€1,000 per farm per year will be created. The sale of land by small farmers who cease agricultural activity to other farms willing to restructure their farms will be encouraged.

Conclusion

The policy developments of the last two decades demonstrate, in contrast to persisting public perception, the extent to which the CAP has changed over time. However, this time the discussion about the future financing needs of the EU is taking place during the implementation of austerity measures in many Member States. In this context the question arises of whether or not agriculture can be exempt from the proposed attempts to save money. When the heads of state and government approved the continuation of agricultural spending until 2014 at the Brussels summit of October 1999, they also approved direct payments to the accession countries and thereby made accession possible in the first place. This gave agriculture the guarantee the sector needed to make plans until 2014. This period of relative planning stability until 2013–14 gave the sector sufficient time to actively undertake structural reforms. However, because today about two-thirds of

agricultural workers in Europe are 55 and older, European agriculture is now confronted with an unavoidable structural transformation. In this situation it is no longer acceptable to cushion the fact that structural changes are unavoidable.

Another point of criticism, this time stemming from the agricultural sector itself, finds fault with the number of different regulations in each Member State, because in this way the commonality of the agricultural policy is given up or at least undermined. Here, one should be realistic: in an EU of soon to be 28 members, there can be no detailed, unified solutions for all. In other areas this has been the case for much longer, but in the case of the CAP, this was papered over with more money for all in practically every reform until 1999. Now, however, the EU budget is getting tighter, and at the same time the range of special interests is ever greater. National and regional responsibility for the general framework is becoming more important for agriculture.

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[9] In Article 20 of the part of the Marrakesh Agreement that deals with agriculture, it had been decided that a renewed round on agricultural trade would be called no later than 1999, with the goal of further liberalisation.
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[11] European Commission, 'Agenda 2000: A CAP for the Future', *Common Agricultural Policy: Review 1999* (2000), 8–9.
[12] Council Regulation (EC) no. 73/2009 of 19 January 2009 establishing common rules for direct support schemes for farmers under the Common Agricultural Policy and establishing certain support schemes for farmers, OJ L30 (31 January 2009), 16, Art. 68.
[13] The EU15 are the first 15 countries that became members of the European Union: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden and the United Kingdom.
[14] 'As its name suggests, it is a method of mobilising and delivering rural development in local rural communities, rather than a fixed set of measures to be implemented', European Commission, Directorate-General for Agriculture and Rural Development, *The Leader Approach: A Basic Guide* (2006)
[15] Council Regulation (EC) no. 73/2009 of 19 January 2009 establishing common rules for direct support schemes for farmers under the Common Agricultural Policy and establishing certain support schemes for farmers, OJ L30 (31 January 2009), 16.
[16] Chaptalisation is the process of adding sugar to unfermented grapes in order to increase the alcohol content after fermentation.
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[18] European Commission, *The CAP Towards 2020: Meeting the Food, Natural Resources and Territorial Challenges of the Future*, Communication, COM(2010) 672 final (18 November 2010).
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[20] Ibid.

[21] Ibid.

[22] Ibid.

[23] European Commission, 'The European Commission Proposes a New Partnership between Europe and the Farmers', Press Release (12 October 2011), accessed at http://europa.eu/rapid/press-release_IP-11-1181_en.htm on 12 February 2013.

[24] Ibid.

[25] In order to explain the 10 key points of reform, Commissioner for Agriculture and Rural Development Dacian Cioloş introduces each of the points in a short video accessible via each of the links referred to in the key point: http://ec.europa.eu/agriculture/videos/reform/key1_fr.wmv

[26] http://ec.europa.eu/agriculture/videos/reform/key2_fr.wmv

[27] http://ec.europa.eu/agriculture/videos/reform/key3_fr.wmv

[28] http://ec.europa.eu/agriculture/videos/reform/key4_fr.wmv

[29] http://ec.europa.eu/agriculture/videos/reform/key5_fr.wmv

[30] http://ec.europa.eu/agriculture/videos/reform/key6_fr.wmv

[31] http://ec.europa.eu/agriculture/videos/reform/key7_fr.wmv

[32] http://ec.europa.eu/agriculture/videos/reform/key8_fr.wmv

[33] http://ec.europa.eu/agriculture/videos/reform/key9_fr.wmv

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European Structural and Cohesion Policy

Introduction

European structural policy and European cohesion policy are often referred to in abbreviated form as regional policy. In practice, however, all three are related in terms of their shared concern for strengthening cohesion across the regions of Europe.

Regional policy is an investment policy for all of Europe's regions; it aims not only to reduce disparities in economic prosperity across regions within the EU but also to provide for increased economic growth and employment in all its regions. Proactive structural and cohesion policies contribute to the attainment of these goals.

Although the Preamble to the Treaty of Rome refers to the need 'to strengthen the unity of [the European] economies and to ensure their harmonious development by reducing the differences existing between the various regions and the backwardness of the less favoured regions', a system devoted to the implementation of a regional policy did not exist at the time of the Treaty's implementation.

In the wake of the accession of the UK and Ireland in 1973, the necessity of assisting structurally disadvantaged regions and of promoting cohesion between regions became particularly evident. Since 1975 and the establishment of the European Regional Development Fund (ERDF) as a means of helping the less prosperous regions improve their economic performance, and particularly after the accession of Greece, Spain and Portugal in 1986, regional policy has progressively developed to become one of the most important EU budget items. With the eastward enlargement of the EU in 2004 and the accession of Bulgaria and Romania at the beginning of 2007, economic and social disparities across the individual regions of the EU have increased considerably. This tendency has continued as a result of the current national budget crises and is

reflected, for example, in the significant increase in unemployment in some regions in Europe. At the same time, however, along with regional disparities, eastward enlargement has also led to increased development within specific regions of the EU.

The figures published in March 2012 by Eurostat, the statistical office of the European Union, on per capita gross domestic product (GDP) render the economic disparities between the regions immediately apparent.[1] Statistically, in terms of 2009 per capita GDP, Bulgaria is the poorest Member State of the Union; in terms of purchasing power Bulgaria is six times weaker than the wealthiest Member State, Luxembourg, which generated 266.3% of the average per capita GDP of the EU. Still greater disparities are evident when individual regions are compared separately. Whereas the Severozapaden region in Bulgaria produces 27% of per capita GDP in terms of purchasing power, the 'Inner London' region of the UK produces 332%. Large differences are also visible in the figures concerning rates of unemployment, in particular with regard to individuals less than 25 years of age.[2] Whereas the rate of unemployment for those under 25 is 7.9% in Austria, it is 46.2% in Spain. Furthermore, although the regions within the London–Hamburg–Munich–Milan–Paris area cover only 14% of the EU territory and only a third of the European population (approximately 34%), they produce more than 40% of the EU GDP and are responsible for three quarters (75%) of investments in research and development. These statistics indicate the discrepancies in terms of competitive power within the EU. This is made still clearer upon consideration of the EU Regional Competitiveness Index of 27 February 2012,[3] which provides a synoptic representation of the territorial competitive power of the so-called 'NUTS 2 regions'.[4] Amongst the 10 most competitive regions of the EU are the three Dutch provinces of Utrecht, North Holland and South Holland, along with Hovedstaden, London and Helsinki. Moreover, in some Member States there is a large gap between the capital regions and the hinterland. In future, this could lead to increased pressure on the capital regions and to the under-utilisation of resources in less developed regions.

The Structural Funds and the Cohesion Fund form the backbone of European regional policy. They are managed by the European Commission's Directorate General for Regional and Urban Policy (REGIO). However, the activities of DG REGIO are not limited solely to administering these funds. Its general purpose is to strengthen economic, social and territorial coherence ('cohesion') across the EU. The European regions and their cities are subject to continuous transformation. As a result, the proposals and actions of the structural and cohesion policy of the EU must reflect these changes in terms of organisation. DG REGIO is responsible for conducting this process and for suggesting appropriate courses of action.

While the political targets are set at the European level as well as at the national level, the specific implementation of regional policy takes place at the national or regional level and is organised differently from country to country according to the local needs of the various Member States. In general, however, it is carried out in the regions in consultation with the Commission and the national governments. Each Member State, together with the European Commission, agrees on one or more Operational Programmes for each fund for a seven-year period, as do those regions that have their own Operational Programmes (not all do). Operational Programmes set the priorities for each fund and describe the fields of activity that will be funded, as well as the relevant interventions and their objectives.

The establishment of the relevant Operational Programmes proceeds on the basis of the Community Strategic Guidelines on cohesion and the National Strategic Reference Framework.

To improve the classification of the territorial units within the EU, a system of unified statistical levels entitled NUTS ('nomenclature of territorial units for statistics') has been established.[5] By means of the NUTS classification system, the economic territory of the Member States, including their transnational areas, has been subdivided. The NUTS levels are determined according to population size. Each Member State contains three vertical levels.

In terms of regional policy, development funds are provided to specific NUTS regions, above all at the NUTS 2 level. At the NUTS 2 level, the 27 Member States of the EU have been divided into 271 regions which generally correspond with national administrative units.

At the beginning of the programme period in 2007, the European structural and cohesion policy took as its basis the 2001 Treaty of Nice. Since the ratification of the Lisbon Treaty (the Treaty on European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU)), expanded rules have been applied. Article 3(3) of the TEU states:

> The Union . . . shall work for the sustainable development of Europe based on balanced economic growth and price stability, a highly competitive social market economy, aiming at full employment and social progress, and a high level of protection and improvement of the quality of the environment. It shall promote scientific and technological advance. . . economic, social and territorial cohesion, and solidarity among Member States.

Accordingly, Title XVII of Part Four of the TFEU is now devoted to 'Economic, social and territorial cohesion'. Articles 174–8 on regional policies and structural funds (replacing former Articles 158–62 of the Treaty on European Community) contain individual changes. The Community goal of territorial cohesion, previously pursued through the promotion of cross-border cooperation, is now explicitly accompanied by economic and social cohesion in Article 174(1) of the TFEU. Furthermore, in Article 174(3) of the TFEU, the eligibility of specific regions is made clear. Of particular importance in this context are the rural areas that have been affected by industrial transformation as well those that have been disadvantaged by difficult, long-term natural or demographic conditions (for instance, the most northern regions that have a very low population density and the island, border and mountain regions). In the past, these regions had already received targeted support. The Treaty of Lisbon thus codifies the existing principles of distribution. The regulations concerning cohesion policy fall under the ordinary legislative procedures (Articles 177 and 178 of the TFEU).

Current structural and cohesion policy (2007–13)

Fundamental principles and the method of calculation

The current structural and cohesion policy is set for a period of seven years (2007–13). The funding targets and general guidelines of the structural and cohesion policy were established in the five Structural Funds Regulations which were adopted as a package by the Council and European Parliament (EP) in July 2006.[6] They constitute the legal basis for the funds. The regulations also lay out the structure by which the funds are calculated and the means by which they are distributed according to the respective instruments. The allocation of funds depends on relative regional and national prosperity, the population and the rate of unemployment.

In addition, financing during a given funding period is limited to a maximum of approximately 4% of the GDP of the Member State.

In order to achieve targets such as a reduction in differences in standards of living across Europe's regions and an increase in growth and employment, the EU has allocated approximately €347 billion for cohesion and regional development for the current financial period. This amounts to approximately 37% of the overall EU budget (approximately €925 billion).

Objectives

European structural policy has always been based on the idea of solidarity between prosperous and less prosperous regions. Thus, the Member States with wealthier regions contribute more to the budget of the EU and thereby foster the economic development of the 'poorer' regions and Member States. Another basic goal of the Community is to strengthen cross-border economic and social cohesion. The investments made in the context of the structural and cohesion policy are thus necessarily focused on economically weaker regions. By offsetting their locational disadvantages, regions are to be enabled to participate in Europe's overall economic development, which will reduce regional disparities. Moreover, a

successful structural and cohesion policy will contribute to the strengthening of competitiveness across the entire Community. Solidarity between the stronger and the weaker will thereby produce further economic progress.

This is why the European regions have been divided into two categories for the current funding period: the Convergence regions and the Regions of Competitiveness and Employment. As in the previous funding period, the GDP is decisive in determining the classification of the regions. Convergence regions have a per capita GDP that is lower than 75% of the Community average.

In addition, funds for a further objective—European Territorial Cooperation (ETC)—are made available under the condition that the recipient region borders a Member State or a third country.

Convergence

The Convergence objective refers to the development and structural adjustment of lesser developed regions. Within the 27 Member States of the EU, there are 84 regions in 18 Member States which fall under the Convergence objective (effective 2011). One hundred and fifty-four million inhabitants live in these regions. The economic development of these Convergence regions is a top priority on the political agenda of the EU. These are regions which are characterised by high rates of unemployment, low levels of investment and poorly developed infrastructure.

The EU's average GDP has dropped considerably as a consequence of the EU's eastward expansion, as almost all of the new Member States have remained far below the 75% limit since 2004. Due to this statistical effect, 16 regions in Belgium, Germany, Greece, Spain, Italy, Austria, Portugal and the UK have risen above the 75% limit and thus have become 'phasing-out regions'. As such, during the funding period to 2012, these regions received transitional support in the context of the Convergence objective.

For the convergence regions, approximately €280 billion has been allocated, of which approximately €70 billion is derived from the Cohesion Fund and approximately €210 billion from the ERDF, a sum which accounts for more than 80% of the total budget of the ERDF.

According to Commission estimates, the resources provided by the structural and cohesion policy in the 2007–13 period will generate additional growth in the less developed regions of up to 10% and create as many as 2.5 million new jobs across the entire EU.

Regional Competitiveness and Employment

The remaining 168 regions in 19 Member States with a population of 314 million inhabitants will receive funding in the context of the Regional Competitiveness and Employment objective (previously objective 2). Here, too, there are 13 regions distinguished by particular characteristics. The 'phasing-in' regions are to receive particular financial allocations because they fell under the Convergence limit in the previous funding period. Included here are, for example, the Republic of Cyprus, the Canary Islands and the Valencia region. Approximately €55 billion has been allocated for the stabilisation of per capita GDP over the 75% limit.

The funding for this objective is intended to raise existing levels of competitiveness and both to secure and to create an attractive environment for research and innovation, which in turn will foster the transition to a knowledge-based society.

European Territorial Cooperation

Along with Convergence and Regional Competitiveness and Employment, a third objective of the European structural and cohesion policy, ETC, has been included which, in the current funding period, will be financed entirely by the European Regional Development Fund. This objective emerged from INTERREG, a Community initiative established in 1990. In support of regions bordering other Member States or third

countries, ETC has been allocated €9 billion for the 2007–13 period, a budget which is considerably higher than that allocated in the previous funding period. ETC is based on three pillars: cross-border cooperation (comprising 74% of the budget), transnational cooperation (21% of the budget) and interregional cooperation (5% of the budget).

ETC affects 181.7 million (37.5%) EU inhabitants. The funding areas are currently divided into 52 cross-border programmes based along the internal borders of the EU and which promote, above all, trade, tourism and culture. Further to this are 13 transnational cooperation programmes for the joint development of geographically large areas such as the Baltic Sea and the Alps. In the context of interregional cooperation, relevant regional authorities form networks for the exchange of best practices and for the implementation of projects.

Funding instruments

The EU funds its structural and cohesion policy primarily through the Cohesion Funds and the two Structural Funds (the European Regional Development Fund and the European Social Fund). In addition to this are other initiatives that have been developed by the DG REGIO together with the European Investment Bank.

In the interests of providing a comprehensive review, it should also be noted that two other special Structural Funds exist which are intended to balance out the sectoral specificities found in agriculture and fisheries: the European Agricultural Fund for Rural Development (EAFRD) and the European Fisheries Fund (EFF). These latter two funds will not be discussed further in this chapter as they are to be included within the purview of EU agricultural policy from the current funding period (2007–13).

The Cohesion Fund

In principle, the Cohesion Fund (CF) is not a Structural Fund as it is implemented at the national level by the various Member States. Established

by the Maastricht Treaty, it became operational in 1993 as a means of providing support to economically less developed Member States and thereby of improving the economic, social and territorial cohesion of the EU. In the present funding period, it has been allocated a budget of approximately €70 billion. In contrast to the Structural Funds, the CF displays several specific features.[7]

First, it is intended for application within the least prosperous (i.e. economically weakest) Member States. Eligibility is restricted to Member States with a per capita GDP of less than 90% of the Community average. Included here are all the regions in the 12 Member States that acceded in 2004 and 2007, as well as Portugal and Greece. Spain was also eligible for funding from the Cohesion Fund during a transitional period. In total, one-third of the population of the EU lives in a Member State funded by the CF. A calibrated scale within the relevant regulation ensures that more funding is allocated to the least developed within this group of EU Member States.

Second, only individual initiatives related to the expansion of the trans-European infrastructure and transportation systems, as well as the sustainable development of the environment, are eligible for support from the Fund. The intention of the Fund is, above all, to improve infrastructure in the Member States by means of growth-oriented investments in transportation networks and environmental projects. With regard to the environment, energy and transportation systems are to be promoted provided that they are advantageous to the environment. Of relevance here are projects related to the production of efficient uses of energy, renewable energy and the strengthening of public transportation systems. With regard to infrastructure, national projects are preferred that are of trans-European relevance and demonstrate European added value, such as the expansion of transportation and railway networks.

Third, the Cohesion Fund (in the current funding period) is subject to ‘macroeconomic conditionality’. According to the current regulation, resources from the CF may be suspended or withdrawn if a Member State

allows its public deficit to exceed 3% and the Council of Ministers determines that its proposed remedial measures have failed to show sufficient effect.

As with the Structural Funds, the resources of the EU are to be used in a context of co-financing with resources from the Member States. For the Cohesion Fund, the maximum amount of financing from the EU is set at 85% of eligible expenditures.

The European Social Fund

The European Social Fund (ESF) was established in 1957 by the Treaty of Rome and is thus the oldest instrument of structural and cohesion policy. It is the EU's most important instrument in employment policy. For the past 50 years, despite the changes that have come with the passage of time, its goal has remained to assist the unemployed to reintegrate themselves into the labour market and to provide them with viable career prospects and, moreover, to improve the career prospects of those already employed. This fund thus plays an important role in assuring economic and social cohesion in Europe. For the current funding period, the ESF has been allocated a budget of €75 billion. The Fund is intended to contribute to the anticipation and remediation of problems associated with economic and social transformation.[8] For the current funding period, the EU has resolved to implement ESF resources in support of employers and employees in their efforts to respond to the innovations of economic change, to improve access to the labour market, and to help prevent long-term unemployment and youth unemployment. Furthermore, funding is to be used to promote longer participation in the labour market, improvements in social integration and the prevention of discrimination, as well as the improvement of work-training and the support of partnerships, confederations and projects. In the context of the above-noted operational programmes, the regions are to establish priorities intended to respond to local conditions and needs.

All regions of the EU are eligible for support from the ESF. However, priority is generally accorded to the structurally weak Convergence regions

with their frequently high rates of unemployment. In the current funding period, approximately 80% of funding has been allocated for use in these regions. A significant portion of this is intended for capacity building, including educational and networking initiatives and the strengthening of social dialogue. Financial support for projects can be applied for and implemented by both public institutions and private businesses. At present, there are more than 10 million people affected by projects supported by the ESF.

As a Structural Fund, the ESF is organised according to the principle of co-financing, although the upper limits vary. In Regional Competitiveness and Employment regions, ESF co-financing may equal 50%, while in Convergence regions, it may total as much as 75% or even 80% for those regions located in one of the Member States eligible for assistance from the Cohesion Fund (Greece, Spain, Ireland and Portugal) and 85% for the most remote regions.

The European Regional Development Fund

The ERDF is a structural fund that has been in existence since 1975. For the 2007–13 period, it has a budget of approximately €272 billion, making it the most potent instrument of structural and cohesion policy in financial terms.

The establishment and growth of businesses plays an essential role here. The ERDF utilises its resources to promote infrastructure, to create jobs, and to support small and medium-sized enterprises (SMEs).[9] It also supports local development projects and the improvement of the environment. To help generate growth, innovative projects are supported which foster higher productivity, the capturing of new markets and international orientation, as well as business relevant infrastructure. In this way, long-term employment is to be created and sustainable economic development ensured. In the development of infrastructure, the focus of support is to promote the 30 priority undertakings of the Trans-European Transport Networks (TEN-T) which support construction projects in the Convergence regions and will lead to the creation of a sustainable balance between road, rail and water

transportation. Ultimately, this is also intended to enable the better integration of the EU's peripheral regions.

In addition, the knowledge-based economy will continue to be promoted. The goal is to raise the innovative potential of the regions by strengthening research centres and thereby creating more positions for highly qualified personnel. The transition to an information and knowledge-based economy, which for many regions is difficult, is to be hastened through the use of ERDF resources. In comparison to the previous funding period, this focus has received greater assistance. The linkage of knowledge and economy will be fostered through support for the formation of networks and clusters. Through support for integrated urban development, the role of cities as centres of economic growth and employment will be strengthened while simultaneously reducing concentrations of poverty and unemployment in the areas on the urban periphery.

The ERDF can also contribute to urban development by means of a programme of integrated cooperation in support of urban renewal (previously URBAN II). Thus, there is the Joint European Support for Sustainable Investment in City Areas (JESSICA) initiative, which is an instrument for the delivery of 'revolving funds' developed by the Commission in cooperation with the European Investment Bank. JESSICA supports projects of regeneration and sustainable urban development through innovation and growth, and was established with the increased participation of private and public financial institutions in the financing of the structural programme, as well as with increased public–private partnerships (along with the JEREMIE (Joint European Resources for Micro to Medium Enterprises) programme in support of SMEs).

Furthermore, the resources intended for the promotion of European Territorial Cooperation[10] will be derived, as indicated above, entirely from the ERDF.

The ERDF is also available to all regions, although here too Convergence regions are to receive greater financial support than Regional Competitiveness and Employment regions.

As a structural fund, the ERDF, like the ESF, is designed on the principle of co-financing.[11]

Changes in response to the financial and economic crisis

As instruments of European solidarity, the Cohesion Fund and the two Structural Funds—the ESF and the ERDF—are playing an important role along with the 'rescue packages' in supporting those Member States of the eurozone currently experiencing financial difficulties.

Due to the changed financial situation in some Member States the Commission—together with effected Member States—has developed strategies to increase administrative capacities and to ensure the more rapid deployment of resources. These measures are intended, above all, to increase the absorption rate of the funds.

On 26 November 2008, the Commission unveiled the European Economic Recovery Plan as a means of both fostering investments and supporting the unemployed.[12] As part of this plan, in several Member States the re-programming of funding has taken place, for example, in the opening up of structural funds for energy efficiency in housing.[13]

The legal basis of the structural and cohesion funds has also been changed to ensure the quicker delivery of funding. Increasing the co-financing rates has also simplified procedures and provided more flexibility.

In June 2010, the EU adopted a series of measures intended to simplify the administrative regulations governing the Structural Funds and the Cohesion Fund.[14] The intention was to ease access to available resources as a means of quickening the local implementation of projects and of imparting greater dynamism into the investments of the European economy. These measures have included, among others, the introduction of a single threshold of €50 million for all major projects in need of authorisation from the Commission and also the possibility of financing major projects via various regional programmes: for example, the construction of an extended section

of highway passing through several regions. Further initiatives include simplification measures and the extension to individual Member States of advanced payments totalling €775 million to offset liquidity problems. This measure benefited those Member States that had received loans in the context of an IMF programme to support their balance of payments and whose GDP had fallen by more than 10%: Estonia, Latvia, Lithuania, Hungary and Romania. These emergency measures also included the suspension of the cancellation of funding commitment according to the 'n+2' rule (EU15) and 'n+3 rule' (new Member States) for the 2007 commitment tranche. According to this rule, resources that had been allocated in 2007 but not dispensed by the end of 2009 or 2010 were to be returned automatically to the EU budget. These changes allow funds allocated in 2007 to be utilised over a longer period of time. Efforts such as these were extended throughout 2011 and 2012. Shortly after government officials from the eurozone had agreed at a special summit on 21 July 2011 to focus Structural Funds on innovation and growth, as well as the promotion of employment and education, the Commission presented several proposals for regulations which would provide for the alignment of the systems of EU co-financing with the ERDF, the ESF and the Cohesion Fund, as well as the European Maritime and Fisheries Fund and the EAFRD. For example, with these changes, Greenland, Ireland, Portugal, Romania, Latvia and Hungary were to have advance access to €2.9 billion from various funds. According to the Commission, the resulting relief to the national budgets was to lead to further projects which would stimulate the economies and increase competitiveness in the affected countries. Included here are initiatives such as the retraining of the labour force, the establishment of business clusters and the development of transportation networks.

An example of the above described 'macroeconomic conditionality' of the Cohesion Fund is the proposal for a Council Decision concerning the suspension of commitments from the Fund for Hungary.[15] This Decision proposed the suspension of €495 million of Cohesion Fund resources allocated to Hungary for 2013 (e.g. 29% of the 2013 instalment). The Council determined that Hungary was showing an excessive deficit and that no effective measures had been taken to reduce it.

In terms of the Structural Funds, the amount of the total allocation for the programme period 2007–13 will remain unchanged. Despite the activities that have been undertaken in the meantime, the absorption of resources has not been equally satisfactory in all Member States. This is evident in the implementation of transnational and interregional cooperative projects which have been difficult to organise.

The preparatory phase for the next programme period (2014–20)

The preparatory phase for the new funding period started at the European level with the presentation of the Commission's *Fourth Report on Economic and Social Cohesion* on 30 May 2007.[16] Along with a detailed analysis of all of the regions (an evaluation of EU cohesion policy 2000–6), it also posed a series of key questions intended to foster debate concerning the future direction of regional policy after 2013. In the context of a self-administered consultation process, over 100 submissions were presented to the Commission. A first analysis has shown that the Commission has considered extending the current eligibility criteria for competitiveness and for employment in the direction of climate change, energy security and demography.

Noteworthy in the context of city planning in the new funding period was an informal ministerial meeting which took place during the German EU Council Presidency in May 2007. The Leipzig Charter was ratified at this meeting. The goal of the Charter is the creation of a common approach to urban construction policy and integrative urban development which would counteract the isolation of disadvantaged neighbourhoods and promote social equality. Urban residential, commercial and leisure neighbourhoods are to be more effectively integrated with each other as a means of avoiding the emergence of one-dimensional and crisis-prone areas such as oversized commercial centres. In this way, the needs of various interest groups are to be more fairly represented in urban development and cities made safer and more future oriented. Through the

establishment of priorities, resources may be better allocated, thereby ensuring the optimal use of the financial resources of both Structural Funds.

The state of transnational linkages within the EU was presented with the submission of the Commission's *Green Paper on Territorial Cohesion* in October 2008.[17] At the time, it was revealed to be a key area that was to play a still stronger role in the future. According to the Commission, increased economic activity brings with it an increase in negative effects such as environmental pollution and social exclusion. With the increased participation of the regions in economic initiatives, a better balance between the urban and rural areas is to be achieved. Furthermore, significant differences remain with regard to the integration of various areas into infrastructure systems. In this regard, by means of Structural Funds, the EU is to increase support for projects to develop the TEN-T in order to create the necessary parameters. Ultimately, transnational problems will only be solved through intensive cooperation at various levels. New forms of partnerships are to help in promoting the necessary exchange.

In the context of a process of consultation initiated by the Green Paper, almost 400 submissions were presented to the Commission and subsequently underwent comprehensive analysis.

In a Commission Staff Working Document, *Regions 2020: An Assessment of Future Challenges*, the prerequisites for the regions in 2020 were examined and assessed.[18] By means of four indicators, the report proposed a risk index which indicated the degree of risk for the regions with regard to future transformations. The report concludes that the EU's strategic parameters need to be adjusted in order to assist the regions in meeting the challenges of 2020. In order to fulfil the multifaceted tasks, each of the regions will have to develop solutions tailored to their specific needs.

Of particular note here is the Barca Report of April 2009 on the financing and future structure of regional policy.[19] Commissioned by DG REGIO, this report comes to the conclusion that 'the Union needs a policy

for economic and social development tailored to the specific needs of very diverse places'.[20] The report identifies 10 specific pillars, including ‘an innovative concentration on core priorities' and 'strengthening the tax mechanisms for core priorities', as well as ‘promoting experimentalism and mobilising local actors’. A pillar ‘refocusing and strengthening the role of the Commission as a centre of competence', along with new forms of contractual agreements between the Commission and Member States, was also suggested.[21] The Commission’s proposals of 6 October 2011 largely adopted these suggestions.

In 2009 the discussion centred—as it does today—on two separate levels. The future financing of cohesion policy was discussed in light of, on the one hand, the discussion concerning resource allocations over the coming multiannual financial framework and, on the other, against the background of the various positions of Member States with regard to the future funding situation. For the years 2009–11, consideration was given to the possibility of focusing exclusively on the funding of the poorest regions, which would have entailed cessation of regional funding for Competitiveness and Employment. Furthermore, there was considerable disagreement within the Commission itself concerning the value and effect of the initiatives of cohesion and structural policy in terms of general European added value. The second level of discussion was, and remains, the question of the organisation of structural and cohesion policy in terms of specific content. Of relevance here was, first, the issue of using GDP per capita as the sole limiting criterion for distinguishing between Convergence and Competitive regions, but also the question of the possibility of including other indicators in addition to the GDP in the measuring of economic performance. There was further discussion concerning the political priorities (at this time still the priorities of the Lisbon Strategy) and over legislative principles and financial instruments (e.g. the increased use of revolving funds), as well as the simplification of the procedures for the simultaneous optimisation of control systems. Although the Commission presented its proposals on 6 October 2011, the current legislative process has revealed that the questions that were then raised have not yet lost any of their explosive character.

The discussion concerning the specific contents of the policy really began with the presentation of a first draft of Europe 2020 (the successor to the Lisbon Strategy which also served as the guideline for the current funding period) and was intensified after its adoption by the European Council in June 2010. The Europe 2020 growth strategy has identified the smart, sustainable and inclusive growth as its priorities and has established concrete statistical targets which are to be met by 2020:

- increase employment for 20 to 64 year-olds from the present rate of 69% to 75%;
- increase in investments in research and development from the present rate of 1.9% of GDP to 3%;
- 20-20-20 targets: reduction of greenhouse gas emissions by 20% from 1990 levels; increase of 20% in the use of renewable sources of energy; reduction by 20% in energy consumption; and
- increase the number of 30 to 34 year-olds with post-secondary education from the present rate of 31% to 40%; reduction by 20 million of the number of people at risk of poverty and social exclusion.[22]

In January 2011, DG REGIO published the Communication *Regional Policy Contributing to Sustainable Growth in Europe 2020*,[23] which set out the role of Regional Policy in contributing to the implementation of the Europe 2020 growth strategy, in particular with regard to the creation of smart, sustainable and inclusive growth.

With the conclusions of the *Fifth Report on Economic, Social and Territorial Cohesion: The Future of Cohesion Policy*, the Commission presented the basis for discussion on the future of European cohesion policy after 2013,[24] including at the national and regional/local levels.

In particular, the conclusions promoted the replacement of the current system of phasing-out and phasing-in with a new funding category for those

regions whose economic performance is between 75% and 90% of the EU average as a fairer treatment for regions with comparable levels of development. Enhancing the European added value of cohesion policy, the conclusions also contain ideas for reinforcing strategic programming, increasing thematic concentration and supporting the use of new financial instruments. Furthermore, the Commission mentioned an ambitious urban agenda and the proposed reinforcement of regional approaches to development. With regard to the implementation of programmes and projects, the Commission wants to reduce administrative burdens and simplify the procedures of financial management. These are only some of the important aspects of this report.

Along with the Commission, other European institutions, and in particular the EP, have occupied themselves extensively with the organisation of structural and cohesion policy after 2013. Indeed, the EP exercised great influence on the Commission proposals of October 2011. In October 2010 a plenary session of the EP adopted a resolution on EU cohesion policy and regional policy after 2013.[25] In June 2011 the EP adopted a resolution entitled 'Investing in the Future: A New Multiannual Financial Framework (MFF) for a Competitive, Sustainable and Inclusive Europe'.[26] One of its important aims was the introduction of an intermediate category which would offer affected regions more security in terms of their development and which would also ensure that regions of the EU with similar development levels are subject to the same eligibility requirements. The gap between the regions within the 'more developed regions' category would otherwise be too large.

It is noteworthy in this context that both the Committee of the Regions (CoR) and the Economic and Social Committee have also given this topic intensive consideration since 2010. The CoR was the first European institution to issue a position in this policy area.[27] The CoR argued for the appropriate and realistic further development of cohesion policy after 2013 and campaigned for a sustainable cohesion policy which, ultimately, would be of value for all of the regions but which made less developed regions a particular priority. The CoR had already in June 2011 suggested the creation

of a new 'intermediate' category.[28] The CoR also expressed the hope that 'complementary indicators to GDP can be developed to better illustrate the progress made in reducing the disparities between and within Europe's regions.'[29]

In the context of this discussion, a variety of events, forums and meetings took place in order to foster the most open dialogue possible between all of the stakeholders in the regions. A broad range of studies, investigations and expert advice was also presented. Moreover, a 'High-level Group' on future cohesion policy was established, which between 2009 and 2011 submitted proposals that were addressed in many contributions to the consultation process.

There was broad consensus that the primary goal of cohesion policy must remain the reduction of economic and social disparities within the EU. Structural and cohesion policy ought therefore to continue to concentrate on less developed regions. A majority of the stakeholders also indicated, however, that the policy must apply to the entirety of the EU. Cohesion policy is not simply a mechanism for engendering solidarity but also for strengthening the local development potential of the European regions. The funding of the developed regions nonetheless remained a subject of discussion. An informal network of over 140 regions was thus created by mid-2010. The intention was to promote the continued funding of the more developed regions during interactions with Union institutions. More than 80% of the more developed regions submitted a declaration on 7 October 2010 demanding the continuation of the current and long-term–oriented Regional Competiveness and Employment objective.

This informal network is only one example of a larger number of networks that have been established in the last few years.

The debate at the European level regarding the role of regional policy—whose expenditures have grown—has intensified significantly in the wake of the financial and sovereign debt crisis, which has necessitated the need for budgetary reductions. This debate is gaining in strength due to the fact that

the European Court of Justice has repeatedly identified failings in relation to cohesion policy.

Future structural and cohesion policy (2014–20)

Commission proposals

On 29 June 2011, the Commission presented its proposals for a MFF for the years 2014–20, which for the first time provided an estimate by the Commission of the volume of future structural policy. The Commission Communication *A Budget for Europe 2020*,[30] which is part of the MFF, provides for a budget of up to €336 billion for cohesion policy (i.e. 33% of the entire proposed budget), as well as €40 billion for the Connecting Europe Facility (CEF), a new multiannual financial instrument to finance infrastructure investments in transport, energy and telecommunications.[31] In contrast to this, the cohesion policy budget for the current period (2011 prices) was €347 billion. The Communication contains the following figures:[32]

- Convergence regions: €162.6 billion;
- Transition regions: €38.9 billion;
- Competitiveness regions: €53.1 billion;
- Territorial Cooperation: €11.7 billion;
- Cohesion Fund: €68.7 billion;
- Extra allocation for remote and sparsely populated regions: €0.926 billion; and
- Connecting Europe Facility for transport, energy and information and communication technologies (ICT): €40 billion (with an additional €10 billion ring-fenced in the Cohesion Fund).

These figures show a focusing of resources on the least developed regions (Convergence regions) and Member States. The Commission also clearly indicated that it intends to introduce a new intermediary category (Transition regions)

Furthermore, as a means of addressing the issue of the absorption of funding, the Commission proposed fixing the capping rate for allocation at 2.5% (previously approximately 4%) and considering the possibility of an increase (of 10 percentage points above the applicable co-financing rate) in the payments to the Member States with temporary budgetary difficulties.

On 6 October 2011, the Commission presented its legislative proposals for the 2014–20 funding period, which repeat its MFF proposals for structural and cohesion policy. This involves a comprehensive legislative package with the following proposals:

- a Regulation laying down common provisions for the European Regional Development Fund (ERDF), the European Social Fund (ESF), the Cohesion Fund, the European Agricultural Fund for Rural Development (EAFRD) and the European Fisheries Fund (EFF), hereinafter referred to as the Council Provisions Regulation (CPR);[33]

- three specific Regulations for the ERDF, the ESF and the Cohesion Fund;[34]

- two Regulations concerning the targets for the European Territorial Co-operation and the European Grouping of Territorial Cooperation (EGTC);[35]

- two Regulations regarding the European Globalisation Adjustment Fund (EGF) and the Programme for Social Change and Innovation;[36]

- a Communication on the EU Solidarity Fund.[37]

In this way, the European legislative process on the future organisation of structural and cohesion policy began and is due to be completed by 2013. Questions concerning the nature and extent of future structural policy will be resolved through negotiations on the MFF. Here points of contention are emerging between the Council, the European Parliament and the Commission, as well as within the Council, between net beneficiaries and net contributors. The proposals from the above-mentioned legislative package will be negotiated in parallel. The negotiations can only be concluded when the MFF has been finalised. Thus, an agreement is not expected before 2013. By the end of 2013, the partnership agreements will have to be agreed upon and the individual programmes and plans for each region approved in order for the programmes to commence at the beginning of 2014 as planned.

The Commission has planned four stages for the programming process. At the European level, the presentation of a Common Strategic Framework (CSF) is planned. The CSF is to replace the strategic guidelines currently in place until 2013 and convert the EU's most important priorities into concrete initiatives. The Commission presented a working draft of the CSF on 14 March 2012.[38] According to the Commission, it is to apply to all of the five funds in shared management (the Cohesion Fund, the ERDF, the ESF, the EAFRD and the EFF) and thus serve the EU as an instrument for the better coordination of European investment.

The CSF is thus also intended to help the Member States and their regions to determine their strategic direction for the 2014–20 funding period. With the help of the CSF, various funds may be much more effectively combined than the separate packages of strategic guidelines for cohesion policy in the present funding period. This will enable the maximisation of the effect of EU investments. Furthermore, the CSF will help ensure that the targets of Europe 2020 are actually applied to the projects co-financed by the funds. At the suggestion of the Commission, on the basis of this framework, national and regional administrative authorities will be required to determine their partnership agreements which will oblige them to fulfil Europe's growth and employment targets for 2020. Partnership contracts

(agreements) are to be determined between the Commission and the individual Member States.

At the local level, the Commission has proposed integrated and multi-sectoral area-based local development strategies led by local action groups.[39]

As previously noted, one of the goals of structural and cohesion policy is to reduce existing economic, social and territorial disparities between the regions of the EU. In addition, the MFF Communication describes cohesion policy as much more than that: it has an important role in raising living standards for all citizens in Europe.

According to the proposals of the Commission, the cohesion policy is therefore to serve all of the regions in a comprehensive manner.

For the 2014–20 period, the Commission has proposed three categories. As has previously been the case, the least developed regions are to continue to receive the highest priority. This remains those regions with a per capita GDP of 75% or lower of the EU average. According to current Eurostat statistics (based on GDP from 2007, 2008 and 2009), there are 69 regions in the less developed category with a combined population of 120 million people.

In the present Regional Competitiveness and Employment category, there are the more developed regions whose per capita GDP is over 90% of the EU average. According to the Eurostat statistics noted above, this category is made up of 150 regions with a population of 305 million people.

Furthermore, as expected, the Commission has proposed a new category to replace the current phasing-in and phasing-out groups. This is in particular reference to those regions which in the current funding period ending in 2013 belong to the Convergence objective but whose per capita GDP has risen to over 75% of the average of the 27 Member States. As a safety net, these regions are to retain two-thirds of their current allocations. This also includes those regions with a per capita GDP of between 75% and

90% of the EU average, although they do not fall within the Convergence objective in the present funding period. Here, designation in terms of funding is to be measured in terms of GDP. This means that regions with a GDP of close to 90% will receive funding at levels similar to the better developed regions. According to the above-noted Eurostat statistics, this new category comprises 52 regions with a population of over 72 million people, mainly in Belgium, France, Greece, Italy and Portugal.

Thus, the fixing of an upper limit for co-financing with funds from the EU is to be calibrated. The Commission considered capping co-financing rates at the level of 85% in less developed and remote regions (or in certain cases, 80% and 75%), 60% in transition regions, and 50% in more developed regions.

As a step towards simpler access and better coordination, the Commission has proposed a single overarching CPR for the five funds (the Cohesion Fund, the ERDF, the ESF, the EAFRD and the EFF) in shared management from the previous funding period.[40]

The first section of the CPR proposal outlines the subject matter and definitions. The second section lays out the general rules and objectives of relevance to the five relevant funds. They address general elements of strategic and programme planning, such as, for example, the thematic targets in connection with Europe 2020, the rules with regard to the CSF, partnership agreements with individual Member States, and the rules concerning funding eligibility, financing instruments and the principles of administration and reporting. The third section of the CPR proposal contains the general rules concerning the ERDF, the ESF and the Cohesion Fund. In the CPR proposal, the rules concerning the relevant areas of application, the investment priorities and the performance indicators are presented. The following will only discuss the elements of the first section. The second section will be dealt with later in the discussion of the Regulation proposals for the individual funds.

As previously indicated, the Commission intends to concentrate structural and cohesion policy on the Europe 2020 objectives as a means of improving the previous, less differentiated approach. In order to achieve this

degree of concentration, the Commission has proposed the following 11 thematic priorities for all of the 5 funds in shared management:

- research, technological development, innovation;
- information and communication technologies;
- reduction of greenhouse gas emissions in all sectors of the economy, adaptation to climate change, risk prevention;
- environmental protection and natural resource efficiency;
- sustainability in transportation and the removal of bottlenecks in network infrastructures;
- employment, mobility and labour force;
- social integration and combating poverty;
- education, skills and life-long learning; and
- institutional capacities and the promotion of efficient public administration.

These objectives are to be set forth in the Common Strategic Framework and in the partnership contracts (agreements) between the Commission and each Member State. The targets are to be clear and measurable. The Commission wants Member States and Regions to identify indicators from a pre-established list directly linked to the Europe 2020 growth strategy.

The Commission also wants better opportunities for region, cities and local communities to play a more active part. In the CPR proposal, upon conclusion of the partnership agreements, the Member States are to be included in a partnership with, among others, regional and local economic and social stakeholders, as well as representatives of civil society.[41]

Another innovation is the introduction of more robust performance requirements and incentives by means of conditionality provisions. This is to ensure that resources are deployed in a results-oriented manner. The Member States are to receive incentives to utilise resources in a manner supportive of the Europe 2020 objectives. This is to occur in several phases of the process.

At the forefront are the '*ex ante* conditionalities' which must be fulfilled before funds are allocated. This is to ensure that the conditions necessary for their effective support are in place. These provisions have been stipulated together with the criteria for their fulfilment in the draft of the CPR, which contains a comprehensive catalogue of conditions such as, for example, the requirement of prior application of specific EU guidelines, as well as the establishment of certain developmental strategies (for example, strategies regarding 'smart specialisation') and horizontal criteria (for example, on public procurement).

Furthermore, *ex post* conditionality provisions have been suggested which would make the further allocation of resources dependent on the fulfilment of the objectives set out in the partnership agreements. A total of 5% of fund allocations per fund and Member State are to be held as a performance reserve to be dispensed after a programme review during 2019 and demonstration that the intermediate targets have been fully met. Apart from the use of performance-dependent reserves, the non-fulfilment of intermediate targets could lead to the suspension of funding.

The CPR proposal also contains macroeconomic conditionalities to ensure that the effectiveness of the funds is not undermined by unsound macro-fiscal policies. Through the closer integration of cohesion policy with economic policy, the Union intends to achieve a more efficient use of CSF funds. CSF funds may thus be redirected toward the solving of a Member State's economic problems if required.

The funding resources from the above-mentioned EU funds are to be utilised in shared management between the Member States and the

Commission, in keeping with Article 53b of the Financial Regulation of the EU.[42] In concrete terms, this means that Member States themselves implement the funding programmes but that the relevant legislative and administrative guidelines at the national level must comply with the rules and principles established at the EU level. Of relevance here is the establishment at Member State level of management and control systems which conform to the requirements set forth in the General Regulation.

The implementation process, including financial management, is also to be streamlined and simplified through the increased use of measures such as simplified costs, results-oriented payments and a simplified application process for major projects. Furthermore, development in the direction of 'e-Cohesion' is being planned in order to reduce administrative burdens and to improve accountability. Another step in this direction is the planned creation by the end of 2014 of a single information centre where recipients will be able to present all information in an electronic format. As a further example of streamlining, the control of small programmes will be exempt from a Commission review.

For the funds in the third section (the ERDF, the ESF and the Cohesion Fund, which will be dealt with individually below), common rules will be proposed which are intended to restrict the Member States from resorting to multi-fund programmes. Thus, preparation, negotiation, administration and implementation will be packaged together.

A further element is a new system for the general administration and control of funding (evaluation and monitoring) which is increasingly to be oriented towards performance and results.

In its elements, the proposal for the CPR clearly reveals that it is very important to the Commission that future structural and cohesion policy demonstrates European added value. This is to occur through increased mandatory strategic planning with the Member States and the regions, through the application of a thematic concentration of resources for structural and cohesion policy that will contribute to achievement of the Europe 2020

objectives, and also through implementation of the above-noted conditionality provisions. Of importance here is also the undiscussed matter of the introduction of financing instruments (equity investments and loan guarantees).

The Cohesion Fund

As in the past, the Cohesion Fund is intended to help Member States with a per capita GDP which is less that 90% of the EU average to invest in transportation projects and in the environment. In the area of transportation, projects of relevance to the TEN-T are to receive funding, as are those related to low-carbon transport systems and urban transport. In terms of the environment, the Fund will support climate change and risk prevention, investment in the water and waste sectors, and projects that benefit the urban environment. Moreover, projects in the area of energy may also be supported as long as they demonstrate value for the environment: for example, projects regarding energy efficiency or sources of renewable energy.

The European Social Fund (ESF)

The ESF contributes to almost all of the Europe 2020 objectives given that it is intended to make progress towards the achievement of full employment, to increase quality and productivity in labour, to increase the mobility of the EU labour force, to improve career training and to promote social integration. The ESF is also able to contribute directly to the key Europe 2020 objectives:[43] in particular employment, education and the reduction of poverty. For this reason (as indicated above), a stronger thematic concentration is planned for the current period. In order to contribute to integrative growth, future funding is to be focused on the following four thematic objectives:

- support for employment and the mobility of the labour force;
- support for social integration and the reduction of poverty;
- investments in education, qualifications and life-long learning; and

- improvement of the institutional capacity and efficiency of public administration.

These four objectives are to be supported by 18 investment priorities, including the adaptation of the labour force, businesses and entrepreneurs; accessibility to employment for the unemployed and those looking for work through support for employment initiatives; and the promotion of business start-ups and a better work–life balance. According to Commission proposals, priority is to be given to the financing of programmes which concentrate on the top four investment priorities.

For the above-delineated objectives, a rate of concentration of 80% of the resources in more developed regions, of 70% in transition regions and of 60% in less developed regions has been suggested in the proposals.

According to Commission proposals, a further thematic concentration would be the allocation of 20% of the ESF budget of each Member State for the promotion of social integration and the reduction of poverty.

Furthermore, SMEs are to be strengthened, access to ICT improved and the development of an environmentally sustainable economy promoted.

The stipulations of the ESF Regulation[44] are intended to more firmly implicate social partners and non-governmental organisations (NGOs) in the programme planning and implementation of the ESF, particularly in less developed regions. To this end, by means of global grants, methods have been created to involve social partners and NGOs.

The European Regional Development Fund (ERDF)

The ERDF is intended to help reduce disparities between the regions and thus promote economic, social and territorial cohesion. It supports investments in the areas of research and development, innovation, climate change, the environment, SMEs, services of general economic interest, telecommunications, energy and transportation infrastructure, health,

education, and organisations of social assistance, as well as sustainable urban development.

Also with regard to the ERDF, according to Commission proposals, increased thematic concentration will be achieved in future through the setting of funding quotas. Thus, the more developed regions and the transition regions are to receive 80% of ERDF funding at the national level for the promotion of ventures in the areas of energy efficiency and renewable energy, as well as for innovation and the support of SMEs, among others. At least 20% of this is to be utilised for energy efficiency and renewable energy sources.[45]

According to Commission proposals, the regions that no longer fall within the Convergence objective are to be required to use 60% of their funding for energy efficiency and renewable energy, as the Commission assumes that restructuring needs remain in these regions. The remaining 20% will be applicable to the other ERDF priorities.

To this end, the ERDF is to be deployed in support of less developed regions in its full diversity. The Commission has thus proposed that these regions be able to choose from a broad range of investment priorities. These regions are also to implement 50% of their ERDF resources in the areas of energy efficiency, renewable energy and innovation, as well as the promotion of SMEs (6% of which is to be directed towards energy efficiency and renewable energy).

Given that more than 70% of the population of the EU live in cities, in the future the Commission intends to devote more attention to sustainable urban development through the focused application of ERDF resources—although the Commission has no direct authority in terms of urban policy. Nonetheless, for many years the Commission has supported urban development (through the URBAN programme) within the context of cohesion policy, among others. Thus, this approach to the 'urban dimension' is not surprising. From the perspective of the Commission, sustainable urban development assumes an entire series of integrated initiatives such as, for instance, the creation and securing of high-value public spaces, the

modernisation of infrastructure networks and the improvement of energy efficiency, as well as an active policy for innovation and education. Here too the Commission has proposed a funding quota of 5% of ERDF resources for each Member State.[46] The ESF is to be included as a complementary component. According to Commission proposals, the management of these integrative initiatives (programmes) are to be delegated to the relevant cities (that is, one level down, at the local level).

Innovative measures in the area of sustainable urban development will be a further instrument of cohesion policy after 2014. The goal is for cities to propose and implement innovative ideas in terms either of financing or implementation which can then later be used by other municipalities as examples of successful projects. The Commission has proposed reserving 0.2% of ERDF resources on an annual basis for these innovative measures. The administration of these measures is to be managed by the Commission itself.

The Connecting Europe Facility

In the MFF, the Commission also proposed a new facility to support infrastructure investment across Europe, the Connecting Europe Facility (CEF). The following will briefly delve into this proposal as it may be considered a Commission financing instrument for structural policy since it is supported with resources from the Cohesion Fund.

From the Commission's perspective, the CEF will complement the investments made by the cohesion policy in infrastructure in less developed regions and Member States. As a directly managed financial tool, the CEF will fund infrastructure initiatives of high EU interest and added value in transportation, energy and telecommunications.

On 19 October 2011, the Commission presented the Connecting Europe package, which specified the proposals for the MFF that had been outlined on 29 June 2011.[47] Within the new MFF, the CEF is to receive €40 billion, with an additional €10 billion euros ring-fenced in the Cohesion Fund for transport projects. The Commission has emphasised that the transportation

sector will require €500 billion in investments until 2020: €1 billion for the energy sector and €270 billion for telecommunications and ICT. As these infrastructure projects may have a very long lead time in terms of planning and implementation before returns are realised, private investors will have to be found. In the proposal for the CEF, the Commission proposed making more systematic use of innovative financial instruments in the effort to offer alternatives to traditional grant funding mechanisms and to plug financing gaps for strategic investment.

European Territorial Cooperation

Cooperation between affected regions is an effective means of solving transnational difficulties. Cooperation helps avoid the problem of, for instance, individual regions carrying excessively high costs while others incur none (for example, cross-border pollution). Moreover, during the process of cooperation important experience and know-how can be exchanged. Furthermore, the formation of clusters can contribute to the effective solution of specific problems.

ETC is thus one of the objectives of cohesion policy. ETC facilitates co-operation amongst all of the regions of Europe.

The Commission proposal has stipulated the amount of financial resources available for each area and determined the criteria for allocation to the Member States. The resources are to be divided as follows:

- 73.24% for cross-border cooperation;
- 20.78% for transnational cooperation; and
- 5.98% for interregional cooperation.

The challenges facing the Member States and regions are transnational and transregional in nature and demand common action at the relevant territorial level. From the Commission's perspective, a regulation should

provide the national, regional and local stakeholders with fixed parameters for the exchange of information and help them to respond cooperatively to common problems. The regulation ought to establish the practical details and reflect the transnational context of the programmes. It is to set concrete guidelines for the cooperation programmes and projects and ensure that programme partners agree on what type of project they wish to support. Here too, a thematic concentration has been established, along with investment priorities. In order to optimise synergies, the projects are to be developed in close cooperation with the relevant regions and in consideration of the strategies being followed by the Member States.

The proposal also notes the participation of non–Member States in advancing the full potential of cooperation. This, for example, is the approach being taken by the Danube macro-region, where 14 countries are cooperating to develop projects and initiatives that will promote prosperity in an area with 100 million inhabitants stretching from the Black Forest to the Black Sea.[48] There are other such potential transnational programme areas. This entails extending the mechanism for the transfer of resources for cooperation activities to the external borders of the Union (in the context of the European Neighbourhood and Partnership Instrument and the Instrument for Pre-Accession Assistance). These programmes will contribute to greater security and stability on both sides of the EU's borders.

According to Commission proposals, the current budget for ETC is to be increased by almost 50%.

The European Grouping of Territorial Cooperation (EGTC)

The EGTC is an instrument which has already been established in the current funding period on the basis of Regulation (EC) no. 1082/2006.[49] It is to facilitate cross-border cooperation in the area of structural funds.

Currently, over 550 local and regional entities from 15 Member States participate in 26 EGTCs. The EGTCs have particularly established themselves in those areas where the participants have a history of working

together successfully and have recognised the value of the EGTC as an effective instrument for the carrying out of specific projects with the assistance of EU funding.

In the context of the above-noted legislative package, the Commission has also submitted a revision of the present EGTC Regulation. By means of the revisions, clarity is to be achieved with regard to the necessary changes via the Treaty of Lisbon. The basic character of the EGTC, however, is not to be altered. Furthermore, more flexibility is to be introduced. The intention is for the area of territorial cooperation to be expanded through the administration of ERDF funded programmes and through the creation of the legal basis for the participation of non–Member State authorities and regions. The draft of the regulation contains rules and guidelines concerning the inclusion of non–Member States in the EGTC. However, should the situation arise where an EGTC were to be created out of only one EU Member State and a non–member, an additional legal basis for cooperation with a non–Member State would be required in the treaty. Furthermore, the Commission proposes that the acceptance or rejection of the EGTC by national authorities be specified. A limited period of assessment is to be introduced. Because of potential overlapping between existing and future macro-regions, ocean basins and transnational programme areas, the regulation expressly emphasises that transnational cooperation may also be used to promote the development and implementation of macro-regional strategies.

This chapter will not delve deeper into the other regulation proposals put forth by the Commission in the context of the total package of 6 October 2011 as they more properly belong in the category of EU labour and social policy.

Further steps and conclusions

The European legislative process on the organisation of post-2014 structural and cohesion policy has to be completed by 2013. In the coming months the Commission's proposals will be discussed in the Council and the EP.

The discussion in the Council is mainly led by net beneficiaries and net contributors. In this context it also should be mentioned that the return flow to the Member States amounts to approximately 96% of the regional policy budget.

Questions concerning the budget of future structural and cohesion policy will be resolved in the negotiations on the MFF. In these negotiations, there will be a lot of discussion regarding the financing aspects of structural and cohesion policy, such as better spending and flexibility. This is why the negotiations on the MFF are of such importance for the future structure of cohesion policy.

In the discussions regarding the MFF, one of the most important arguments in favour of an adequate budget for the regional policy is its nature as an investment policy for all 271 regions in the EU and the new role of the cohesion policy (especially territorial cohesion) in the context of the Lisbon Treaty. The financing proposals, for instance the ETC and the new CEF, set forth by the Commission indicate that territorial cohesion is seen as an important cornerstone of future structural and cohesion policy.

The proposals from the above-mentioned legislative package for cohesion policy will be negotiated in parallel.

In the meantime, it would appear that in the current legislative process, the perception that the structural funds ought to be of benefit to all of the regions has found acceptance. Many other Commission suggestions on the proposed regulation and the proposal for a Common Strategic Framework are still under discussion, however.

The Commission proposals of 6 October 2011 are not likely to be enacted in their entirety by the Council and EP. Likewise, the working paper on a Common Strategic Framework will, in all likelihood, be subjected to alterations during the course of the legislative procedure. Nonetheless, tendencies already in view, such as the concentration of resources on a narrower field of topics, integrated programme planning and the introduction

of conditionality, as well as elements of more efficient financial control and assessment are likely to find form in the final regulations.

Still open for discussion are issues such as, for example, the future role other indicators can and should play along with GDP in the implementation and assessment of cohesion policy. This assumes, however, that other comparative European wide indicators already exist. The EU Regional Competiveness Index—as a first specific indicator presented by the Commission on 27 February 2012[50]—is perhaps an indication of the direction to be taken by the Commission. This index takes the extent of a region's development into consideration. Moreover, fundamental issues are emphasised in less developed regions, while for the more developed regions innovative capacity plays a larger role. At any rate, the possibility that this indicator will play a role in the future development of regional policy is not to be excluded.

The question of an appropriate balance between control costs and the value they produce also arises repeatedly. Here the proper balance between costs and risks will have to be found.

A further point of discussion is certain to be the partial departure from the present allocation model through the introduction of new financial instruments in cohesion policy such as the CEF. These are intended to increase the leveraging effect of the total budget and to improve fiscal discipline.

The negotiations can only be concluded when the MFF has been finalised. Thus, an agreement is not expected before 2013. By the end of 2013, the partnership contracts (agreements) will have to be agreed upon and the individual programmes and plans for each region approved in order for the programmes to commence at the beginning of 2014 as planned.

As a conclusion, it may be said that, for the future, regional policy is always to be considered in the context of European added value. Due to the current national debt crises, the EU is considering new forms and applications for structural and cohesion policy on all levels after 2013. European financial

resources will have to be more effectively utilised in the future in order to meet the objectives of Europe 2020 and, ultimately, to reduce economic, social and territorial disparities within the EU. The expansion or even continuation of these discrepancies could have negative consequences not only for the internal market but for the entire EU as well as for the common currency.

A new field of special interest will be urban policy and its connection to less developed areas.

Economic globalisation is placing the Member States of the EU under considerable pressure in terms of competitiveness, particularly from the emerging economies of Brazil, China, India, Russia and South Africa. Thus, the aim of European regional policy also has to be to improve the global competitiveness of the regions within the Member States through the creation of technological advantage, smart specialisation and stronger investment in innovation.

Furthermore, the factsheets for all 27 Member States presented by the Commission on 1 March 2012 will be of help in the determination of Cohesion Policy for 2014–20. These sheets outline the progress made by individual Member States with regard to the agreed upon Europe 2020 objectives. They too will arise in discussions regarding future cohesion policy, as the further focusing of structural and cohesion policy on the achievement of the Europe 2020 objectives is inevitable.

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Albrecht Rothacher

The EU's Common Foreign and Security Policy

Introduction

When it comes to international affairs, it is clearly recognised that the EU punches well below its weight. Although it is the world's largest trading power, with 500 million inhabitants and a quarter of the world's gross domestic product (GDP), the EU's external tools have been charitably described as 'smart power': the application of trade privileges (including free trade regimes), economic aid, permanent diplomatic engagement as a multifaceted dialogue and moral exhortations in varying proportions. The effectiveness of these policy instruments is strongest among like-minded countries, such as the members of the European Free Trade Association (EFTA), and among those Balkan and Eastern European countries currently wishing to join the EU. It is also visible in a very limited number of spectacular success stories, such as the Aceh peace accord brokered in 2005 by UN Special Envoy Martti Ahtisaari, or the Ohrid Agreement of 2001, when EU High Representative for CFSP Javier Solana's skills prevented the Former Yugoslav Republic of Macedonia from sliding into civil war and disintegration. Yet, in the geopolitics of world powers—the US, China, India and Russia—the EU hardly figures as a cohesive actor to be taken seriously.

The Treaty of Lisbon tried to address this well-known problem by institutional means, creating a high representative of the Union for foreign and security policy, accompanied by the European External Action Service (EEAS). This agency is composed of merged Commission, Council and seconded Member States' diplomatic staff, and in 2011 also took over the Commission's existing worldwide network of 136 delegations. The high representative chairs the foreign ministers' council and, as a vice-president of the Commission, also takes part in the weekly Commission meetings as a full member of this collegiate body. Hence this new institution is very much *sui generis*, being both intergovernmental and communitarian in structure. This seemingly ingenious compromise is not without consequences and complications. Thus the budget of the EEAS—currently

the EU's external relations are supported to the tune of €4 billion per year—continues to be managed by Commission staff in a special EEAS structure (termed the Foreign Policy Instruments) and remains under the European Parliament's control.

The core issue of unanimity in foreign and security decisions remains, as do the French and British seats on the UN Security Council, which are remnants from the Second World War. Hence the high representative, as in the past, remains very much dependent on the goodwill and the consensus of Member States, their foreign ministers and their heads of government in the exercise of his or her functions and policy initiatives. Whether this institutional reform undertaken by Lisbon will succeed in creating a more coherent and respected EU foreign policy obviously remains to be seen. Growing pains resulting from the merger of distinct administrative cultures and an immediate exposure to real world crises, as in North Africa during 2011, can be expected and will hopefully be resolved in due course. Yet the office of the high representative may require superhuman powers to overcome the structural problems in decision-making and the underlying national differences in world views, strategic interests and tactical preferences among the 27 Member States.

EU strategic interests

Is there a strong core of common strategic European interests, apart from the usual truisms of peace and good neighbourliness? Even in generally Eurosceptic countries, such as Austria, an effective EU foreign and security policy is welcomed by the general public, which knows fairly well the limitations of the EU's national foreign policy and its military.[1] The crux of the matter, then, is the substance of such policies. We could define the physical protection of EU citizens at home and the safeguarding of our common occidental civilisation, our democratic system and the European way of life for future generations as core EU interests. Hence effective EU protection is needed against Islamic terrorism, uncontrolled mass immigration from the

Third World, threats to our energy supplies and against Russia's attempts under Putin to recreate a sphere of influence in its 'near abroad'—which is also the EU's neighbourhood. The EU's security interests are obviously much greater in its troubled neighbourhood, which encompasses the Balkans, the former Soviet Union, North Africa and the Middle East. As early as 1978, Zbigniew Brzezinski rightly described the eastern and southern shores of the Mediterranean as 'an arc of crisis' stretching into the Middle East, Africa and Central Asia.[2] In this region rapid and unchecked population growth has produced a restless, unemployed and undereducated male proletariat, ready to move north and increasingly falling prey to intolerant religious propaganda. The revolutions of 2011 from Tunisia to Egypt are a delayed echo of the 'colour' revolutions of 2000–4 in Eastern Europe, but, being culturally and ethnically further remote from Europe, their outcome remains far from certain.

In principle, the further we move away from Europe, say to Latin America or the Pacific, the less the EU has security concerns. In the age of intercontinental nuclear missiles and trans-border terrorism, addressing certain global security issues remains important, of course. These issues relate to the proliferation of weapons of mass destruction and the possibility of lawless failed states turning into safe havens for pirates and terrorists of the al-Qaeda sort. Addressing such global issues obviously has to be undertaken in the largest possible alliance with third states, notably in partnership with the US.

In addition there are, of course, global interests of an economic and ecological nature, such as saving ecosystems (for example, the rainforests); economising and securing access to raw materials; and preserving a liberal, open trading system for goods, capital and services. After the failure of the 2009 Copenhagen summit on climate change, when negotiators for the EU naively assumed the rest of the world would follow its pre-agreed promises, it now appears as if the tsunami of 11 March 2011, which triggered the Fukushima accident, also flushed away climate change objectives unobtainable in a world without nuclear power.

If we measure current EU instruments and policies against these fundamental strategic challenges, they address them only very partially while

remaining over-engaged in peripheral issues and regions of third-order importance. Organising and subsidising handicraft seminars for tribal women in Nepal or Laos may be all well and good for a charitable non-governmental organisation, but it is not serious foreign policy. In spite of EEAS efforts to the contrary, it is aid programmes of this sort which—encouraged by the Council and the European Parliament—through their cumbersome administration, easily absorb 80% of the manpower and management time of the EEAS and the Commission's external relations staff, both at headquarters and in the delegations. The rest of staff time is spent on technical and trade issues. The sum total is an EU foreign policy hardly worthy of the name.

Public opinion and EU foreign policy

Unlike the response to many other policy fields, public opinion is surprisingly positive about a common foreign and security policy, at least more so than the vested bureaucratic interests in the national foreign and security establishments. In terms of perceived threats, 86% of those surveyed saw terrorism as the greatest security threat, followed by weapons of mass destruction and organised crime (79% each).[3] The 11 September 2001 terrorist attacks, the Spanish train bombings of March 2004 and the London bombings of July 2005 each prompted after-the-fact upsurges in public fear of terrorist attacks, which subsequently subsided until the next incident. In contrast, acceptance rates for a common foreign and security policy have been remarkably stable for decades, with positive views (68% in autumn 2006) three times higher than negative ones (21%). Acceptance is highest in Cyprus and Slovenia (80%) and lowest in the UK (48%), with new Member States being more positive (75%) on average than old ones (66%). So much for Rumsfeld's 'New Europe'. Approval rates for a common defence and security policy, with 75% of those surveyed in favour and only 16% against, are even higher. In this case, British acceptance, at 57%, is even higher than that of neutral Ireland, which, at 52%, is the lowest.[4] In defence and foreign

affairs, 64% want decisions to be taken at the EU level and 32% at the national level. As of spring 2006, the EU's foreign policy conduct was seen as positive by 52% and as negative by 13%.[5]

The EU's rapid intervention force is welcomed by a fairly staggering 68%—especially in Cyprus (88%), Belgium (82%) and Latvia (80%); the least by non-aligned Malta (48%). Its tasks are seen by 71% as the territorial defence of the EU, by 63% as peacekeeping within the EU and by 58% as disaster relief; only 18% view armed interventions in other parts of the world as part of its role. This adherence to a conventional defence strategy is confirmed by a different survey undertaken in neutral Austria. A common European army is accepted here, provided it is used to defend against attacks on EU Member States (60%) or to protect sources of vital raw materials and supply routes (50%); but only 10% want an armed force for war on other continents (with 83% against).[6] Thus, while the project of a European army based on a territorial defence mandate might meet with popular approval, this is clearly not reflected in official EU (let alone NATO) planning. NATO's current fad for long-distance armed interventions is not a vote winner and has little democratic legitimacy. Hence it appears doubtful whether the project of a common European military could ever be borne on the basis of deeply unpopular, costly and often lost joint foreign adventures.

A European army nucleus?

The Common Foreign and Security Policy (CFSP) was created by the second pillar of the Maastricht Treaty in 1993. Like all intergovernmental ventures it has remained undernourished, a sick child compared to the healthy first pillar of Community policies. For some time nothing happened until the UK and France ironed out their differences at the summit of Saint-Malo in December 1998. This opened the door for the European Council in Cologne in June 1999, where the then-15 Member States agreed to strengthen EU security and defence policy by setting up

credible military capabilities and suitable decision-making mechanisms. Six months later in Helsinki, it was agreed to create a rapid deployment force of up to 60,000 men, capable of being dispatched within 60 days to any place in the world for up to one year's duration. These troops do not constitute a European army as their deployment remains a sovereign national decision and thus, to date, has never happened. In June 2000 this military instrument was complemented by a police reserve of 5,000 men and 2,000 civilian specialists for law enforcement and civil protection. The December 2000 Treaty of Nice provided for a proper directing body, a Political and Security Committee (PSC) composed of the senior officials of foreign ministries, that would propose decisions to the Council and be able (in theory) to directly command operations in case of crises. In addition, the chiefs of staff of the 27 Member States form an EU Military Committee for common leadership and planning tasks. Mainly, however, they consult with and give military advice to the civilians of the PSC. There is also a small military staff, which provides early warnings, situation analysis and strategic planning. However it is not known, for instance, what action was taken by this staff during Europe's last military crisis, Russia's short war against Georgia in August 2008. If any action was taken, it remained well camouflaged.

In order to avoid the duplication of work, since 2002—after overcoming the usual Turkish attempts to block the decision—it has also been possible to use NATO structures. This 'Berlin Plus' mechanism was first tried and tested with a joint EU mission to the Former Yugoslav Republic of Macedonia in March 2003. In November 2004, EU defence ministers decided to create 13 'Battle Groups' of mostly mixed nationalities for long-distance peacekeeping operations. Each group is supposed to be 1,000–1,500 men strong; meaning that in reality they are a few battalions thrown together, barely regimental in strength. Hence the battles they face cannot be too severe or last too long. Since 2007 they have even been expected to be able to handle two crises in different places at the same time. Luckily, this has not yet been put to the test.

The limits of soft power

US President Teddy Roosevelt's famous dictum was, 'Speak softly and carry a big stick'. Accordingly, America's youthful imperialism was successful in his time and for decades to come. The EU does the exact opposite: it talks a lot and has no stick. It issues a vast number of moralising declarations on every subject on earth, from the execution of mass murderers in the US to the conduct of elections in Papua New Guinea. Double standards abound. For example, the Palestinians and the Kosovars may be permitted independence (the latter according to most but not all EU Member States), but thanks to the 'One China' principle the Tibetans, Uighurs and Taiwanese are not allowed to harbour national aspirations. Admittedly, once a moral approach has been chosen, it is difficult to remain consistent in light of the realities of power politics. While such an approach may be difficult at times for an institution like the Vatican, for instance, it frequently appears as bigotry in the case of a major international actor such as the EU, some of whose Member States also pursue significant resource and strategic interests, including armed interventions and the sale of arms. As Chris Patten put it, 'It is much easier to wag a finger at nasty Burma than at China.'[7]

For want of a better option, the necessary consensus of the 27 Member States is a more likely possibility when it comes to the use of soft power instruments such as trade concessions, development, governance and financial aid, economic cooperation, scientific and student exchange, structured sectoral dialogues, and summit diplomacy, with their popular photo opportunities, lofty declarations and earnest initiatives. The EU calls this 'smart power' in its public relations brochures, the irrefutable logic being that such programmes are ultimately more economical than military spending and armed conflict. There is no problem with such policies if they are applied by small or medium powers, say, Norway or Iceland. The trouble arises when states are expected to play a larger role in regional affairs or in the world at large. Soft power instruments notoriously fail to impress rough states, such as Iran or North Korea, who are determined to

produce nuclear weapons and carrier missiles. Equally unimpressed are organised lawless non-state operators, such as Islamist terrorists and pirates, or regimes without aggressive external designs but which, like Sudan, Zimbabwe and Burma, are repulsive in the mistreatment of their own people and their national minorities. Many other regimes, including those of Communist Cuba, Laos, Vietnam and China, are not much better and yet, for unexplained reasons, have been spared the horrors of EU soft power sanctions.

More serious, probably, is the fact that the relations between great powers are still primarily defined by geopolitics and power politics. There has been a fundamental misunderstanding if the EU believes that Chinese notions of multipolarity have anything to do with its own cherished notion of multilateralism, where intergovernmentally derived EU norms (which may have first been defined and tested on a greater European scale, such as within the Council of Europe or the Organization for Security and Co-operation in Europe) are then applied universally as UN or other international organisations' rules and as enforceable commitments. China's multipolarity, however, means power politics balanced with mutual non-intervention into the domestic affairs of the big powers (China being one, and the EU having the potential to become one, if it can make it happen). Yet EU strategy papers on China treat multipolarity and multilateralism—mutually exclusive terms—as if they were both mere synonyms for working against American unilateralism.[8]

Worse, in relations with the US the EU is at best seen as a quarrelsome, fairly disorganised junior partner who is most useful when engaging in chequebook diplomacy and not disturbing or changing the US's grand designs. In this respect, US policies and attitudes are not free from their own contradictions: Washington, under various administrations, has regularly complained about EU disunity and the US's tough job of policing the world without a reliable partner. Yet, in the same breath, the US is happy to play divide and rule ('Old Europe' vs. 'New Europe'; the UK's 'special relationship' against the rest, etc.), and reacts defensively and destructively whenever a more united EU appears as a potential rival. US policies fail to grasp that any

real partner (*ex aequo*) by definition has to be independent and have its own effective power base (or else it is not a level playing field), but, as a genuine ally, is not necessarily a rival.

Russia is no longer and India not yet a world power, but their strategic outlooks and mindsets reflect past or aspired-to glories. Hence there is nothing but contempt among their ruling elites for the EU's soft power approach. India's refusal to sign a Partnership and Cooperation agreement and Russia's threats against Estonia and Latvia, its interruption of gas supplies to south-east Europe in January 2009, its two domestic wars against Chechnya, and its war against Georgia in August 2008 all unfolded without a muscular EU response. According to the power politics dominant in the Kremlin, this is an admission of weakness and an invitation to renewed aggression.

In defence of soft power it could be argued that it was soft power—policies of détente, non-aggression, arms control and nominally guaranteed civil rights negotiated in the Commission on Security and Cooperation in Europe (CSCE) agreements, and non-violent opposition, mass disobedience and power transfers negotiated at round-table discussions—which brought about the historic miracle of systemic change in 1989–91 without massacres or a nuclear show-down. The 'colour' revolutions of 2000–4 in Serbia, Georgia, Ukraine and Kyrgyzstan also followed this logic. These methods are excellent and vastly superior to their more violent cousins, when applicable and where appropriate. The trouble is that they do not work in international or domestic politics when the opponent is sufficiently brutal, domestically repressive or bent on aggression externally.

Aid programmes

As mentioned, the EU follows the logic of almost unconditional multilateralism, with the UN and its agencies at the apex of global governance. In this model, the EU operates as a sort of regional implementation agency, which also strives to expand its range from human

and gender rights to emissions controls and, hopefully, global validity. Its instruments are those of commercial policy; financial aid through the European Investment Bank, the European Deference Force and the European Bank for Reconstruction and Development; and development cooperation to a total of €46 billion (including Member States' funds) per year, all embedded in an unceasing cycle of bilateral dialogue and conference diplomacy.

The EU's external policies are haphazardly developed from trade policies (focusing on the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO), with the US and Japan as erstwhile principal trading partners) and development policies (with long-lasting privileges for the African, Caribbean and Pacific countries of the Yaoundé, Lomé and Cotonou agreements; that is, mostly African sub-Saharan ex-colonies). Although many lengthy policy papers have been written, a real strategic logic based on Europe's geostrategic interests is not discernible.[9] Elements abound, but little intellectual, let alone political, effort has ever been made to find coherence and real prioritisation. The multitude of institutional actors and political cross-pressures from Member States, each favouring different world regions, programmes and recipients, has led to a global pot-pourri of subsidised projects in an attempt to make everyone happy. Multiannual cycles of ever-so-well-intended programmes in almost every recipient country support drinking water and waste water projects; protect the rainforest (where it still exists); build new roads; promote trade unions, small businesses, tourism and women's organisations; construct prisons; promote democracy and a free press (if permitted by the host country); and finance any number of consultancies, exchange visits and seminars. Global do-gooding does not come cheap. Thus the EU funds the salaries of the Afghan police (€135 million) to keep them from defecting; hospitals for the poor in India (€110 million); social welfare, ministry payrolls and hospitals in Palestine (€700 million), including the reconstruction of EU-financed infrastructure destroyed by Israel; and various UN operations (€1 billion). The observation and military protection of the Democratic Republic of Congo presidential elections in 2006 alone cost €480 million and, as in the end President Kabila was elected unopposed, it remains unclear what, if anything, the observation achieved. A

new fad is to give budget support as money transfers straight into the recipient ministries' bank accounts. Even in absolute dictatorships this is seriously intended to increase 'democratic accountability'. Supported projects (such as road construction) then have to go through public tenders and, more often than not, are awarded to cheap Chinese bidders, who, with their own workers, quickly deliver often-substandard infrastructure.[10]

When Pakistan became embroiled in serious political turmoil in 2005, the EU's first reaction was to multiply its aid programmes. Predictably, throwing money at trouble spots in an almost-failed state with nuclear arms and huge structural and governance problems could not solve the issue; in fact, Pakistan's security problems have worsened since (which should not, however, be blamed on EU funding). This scattergun approach of well-meant EU initiatives appears sensible if one shares the belief in the universality of the European societal model, especially the dominant Scandinavian gender mainstreaming and political correctness variant. As almost a secular religion, this is for true believers, and heretics are sanctioned. There were certainly success stories during the democratisation of Eastern Europe, Latin America and East and Southeast Asia in the 1990s, but the Brussels(-cum-Washington) consensus is surely not borne out by the realities of most of contemporary Africa, the Middle East, China and Central Asia, for instance.

China has had recent success in Africa, offering credit-financed infrastructure projects, presidential palaces, sports stadiums, new airports, military aid and other facilities which the national elites really desire, with no political strings attached, in return for access to commodities and raw materials.[11]

Given these shortcomings, the magic justification for all EU engagement is 'conflict avoidance'. Are not all these funds, even when mismanaged and wasted, much cheaper and more economical and humane than any nasty, evil and senseless hot war? This would be nice if it were true. Yet the tradition of civil wars in Africa, a continent that for five decades has been a privileged recipient of EU development aid, does not really seem to support this benevolent hypothesis.

Since the EU ties its funds to medium-term programme cycles, its funding is not really suited to rapidly changing conditions. Local power holders (if they care at all) can safely take for granted the flow of funds once they are promised and committed. For instance, despite being the largest single donor and even after a massive transfer exercise motivated by the Barcelona Process and the neighbourhood policy, the EU has not yet managed to persuade its North African partners to stem and intercept the massive tide of illegal migrants crossing the Mediterranean to its southern shores, let alone to take the survivors back in order to deter future, all-too-often-deadly voyages.

The degree of respect which the EU's bureaucratic, appeasing and disbursement-driven approach receives was unfortunately most strikingly revealed by the Congolese reaction to the very valid criticism which Development (now Trade) Commissioner Karel de Gucht made of the military abuses in the Eastern Kivu province and of the general failure to reconstruct governance in Congo. The Congolese Foreign Minister accused him of being 'racist, disrespectful and irresponsible' and declared the Commissioner *persona non grata* in Congo. Yet a Commission spokesman declared subsequently that already-committed aid monies amounting to €300 million would be spent in the country.[12]

Trade policies

The external trade competences of the European Union were defined at the same time as the Treaties of Rome; thus for decades the Community method and majority decision-making have applied. As a result—and in contrast to the CFSP—the EU speaks with one voice, is taken seriously and has had a major positive impact on world trade and on trade-induced prosperity, based on the effective use of comparative advantages. This is by no means a small achievement. In numerous GATT rounds, tariffs have been slashed and non-tariff barriers removed in the interests of Europe's export industries and services.[13] The EU has granted most least developed

countries tariff-free access to EU markets. This is done in the recognition that a successful export performance produces more sustainable development than aid projects, a fact borne out by the series of subsequent Asian success stories, starting with post-war Japan and ending with contemporary China and India.

Unfortunately the Doha Round, which opened in 2001, shows no sign of getting off the ground. For WTO members it was meant to advance growth and trade by providing greater protection for intellectual property and investments, among other things. Yet it remains blocked by large transition countries like Mexico, Brazil and India. In addition, the Obama administration has shown only scant interest in it. In response to this failure, a plethora of bilateral free trade agreements has proliferated, notably in Asia, constituting an ever-more-complicated 'spaghetti bowl' of bilateral rules and privileges that it will be difficult to consolidate later into a multilateral framework within the WTO. It was only with great hesitation that the EU joined this bandwagon outside Europe (for the EFTA countries, free trade has existed in the European Economic Area since 1994) and the Balkans. The initial results include free trade agreements with Turkey, Egypt, Israel, Algeria, Morocco, Mexico, Chile and Korea.

The EU's traditional protectionism for agriculture, after successive policy reforms that have decoupled farm income subsidies from output, is gradually receding. Instruments for commercial defence, such as anti-dumping duties, which had some prominence in the trade disputes of the 1980s, are now only rarely used. Even with respect to China, where the EU's rapidly accumulating bilateral deficits reached the astronomical amount of €170 billion in 2010 and are increasing by €40 million every hour, there is a curious policy restraint, in spite of massive access problems to the Chinese market and a purposefully undervalued yuan, which clearly constitutes currency dumping. This is despite the fact that China is much more dependent on the EU market (as the destination for 21% of its exports) than the EU is on China for our exports (7%). As Chris Patten puts it, with China as its privileged partner, the EU plays a good set of cards remarkably poorly.[14]

National interests

The unanimity principle governing the CFSP would likely make it difficult even to agree on a common luncheon menu were it put to a vote in a Council meeting. Hence the degree to which this policy field has advanced as a common endeavour is remarkable, given its structural defaults (as mission impossible) following the year-long painful stalemates of the Balkan wars of the 1990s. Yet understandably distinct historical ties and geostrategic interests on the part of Member States remain (though the EU claims to have none): those of Spain towards Latin America and the Muslim world; France's ties with the Francophonie and large parts of Africa; the UK's with the US and the Commonwealth, and so on. Sometimes these are neatly complementary, while at times interests and perceptions clash. Take Russia, for instance: a difficult neighbour with post-colonial trauma, and a nuclear and resource power in demographic decline. Some, such as the UK, Sweden, Poland and the Baltics, take a tough principled line to impress the Kremlin's *siloviki* masters, schooled in the thinking of power equations.[15] Others, starting with Cyprus and Greece, but also including Italy, Germany and France, cosy up to them in search of special deals, offering cheap divide-and-rule options on a silver platter. This was highlighted in March 2010 when the French sold four advanced 'Mistral' helicopter carriers to Russia, which, to the audible dismay of coastal Eastern European Member States, will beef up Russia's rapid foreign intervention powers considerably. As usual, differences within the EU were subsequently papered over in platitudinous partnership declarations and initiatives on second-order issues which have left the Kremlin decidedly under-impressed.[16]

Conclusion

When it comes to contentious issues, the EU prefers incremental institutional reforms. Its past record has been one of steady progress against all odds. The Lisbon Treaty has provided for a high representative and the EEAS.

Although at present the prospects for muscular foreign and security policies do not look auspicious, despite the EU's potential as a world power, evolution towards a common army, a merged foreign service and cohesive majority decision-making is by no means out of the question. Under the influence of the Cold War, the EU's founding countries were almost ready for a European Defence Community just eight years after the horrors of the Second World War.[17] A new major external threat from the EU's troubled neighbourhood, be it from the east, the south or the south-east, could again energise a major impulse for a new reform treaty on the external relations front, overcoming the vested interests of the national foreign ministries and defence establishments. As we have seen, public opinion among the 27 Member States would be quite receptive. However, consecutive foreign policy failures might contribute to a change of mind as it is clear that the old division of labour in international affairs—the UK deals with the US, France with Africa and Spain with Latin America, with Germany trying to play the good guy—no longer works. A genuine change, however, is only possible if the EU starts to abolish its unanimity rule in foreign policy decisions and opts for qualified majority voting. Only then will single strategies, not 27 individual ones, loosely coordinated, be feasible.

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Notes

[1] In a survey in October 2002, 77% of Austrians favoured a common European military. Only 17% indicated a preference for separate national armies. See D. Pfarr, *Europäische Sicherheitspolitik und Streitkräfte in der Öffentlichen Wahrnehmung* (Vienna: Schriftenreihe der Landesverteidigungsakademie, 13/2007), 62.

[2] *Time,* 'Iran: The Crescent of Crisis', 15 January 1979.
[3] Quoted in D. Pfarr, *Europäische Sicherheitspolitik*, 17.
[4] Ibid., 31.
[5] Ibid., 35.
[6] Ibid., 65.
[7] C. Patten, *East and West* (London: Pan Books, 1999), 295.
[8] O. Griese, 'EU–China Relations: An Assessment by the Communications of the European Union,' *Asia Europe Journal* 4 (2006), 545–53.
[9] A. Rothacher, *Uniting Europe: Journey between Gloom and Glory* (London: Imperial College Press, 2005), 177.
[10] S. Michel and M. Beuret, *La Chinafrique. Pekin à la conquete du contiment noir* (Paris: Hachette, 2009), 147.
[11] C. Alden, D. Large and R. Soares de Oliveira, 'Introduction', in C. Alden, D. Large and R. Soares de Oliveira (eds.), *China Returns to Africa* (London: Hurst, 2009), 6.
[12] T. Vogel, 'De Gucht Barred from DRC', *European Voice*, 8 January 2010, accessed at http://www.europeanvoice.com/article/2010/01/de-gucht-barred-from-drc/66823.aspx on 9 April 2013.
[13] S. Senior Nello, *The European Union: Economics, Politics and History* (London: McGraw Hill, 2009), 416.
[14] C. Patten, *East and West*, 302.
[15] A. Rothacher, *Stalins langer Schatten. Medwedjews Rußland and der postsowjetische Raum* (Graz: Ares Verlag, 2008), 70.
[16] C. Patten, *Not Quite the Diplomat* (London: Penguin, 2006), 205.
[17] J. Pinder, *The Building of the European Union* (Oxford: Oxford University Press, 1998), 8.

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The Importance of Development Cooperation for the European Union

Introduction

The responsibility for European development cooperation is shared between the EU and its Member States.[1] The European Commission holds that development is at the heart of the external action of the EU. Being both a policy of values—peace, solidarity, the rule of law, respect for human rights—and a policy of influence and interests—having stable, peaceful, prosperous and reliable partners and clients worldwide—EU development policy is very much about investing in Europe's future.

Poverty reduction in the context of sustainable development is the primary objective of EU development policy.[2] Indeed, the reduction, and eventual eradication, of poverty is perceived as a key factor in promoting peace, stability and prosperity in the world, thus allowing the EU to maintain and further strengthen mutually beneficial relations with its partners in all regions.

European development cooperation has been extended gradually, beginning with the Treaty of Rome in 1957, which set up the European Economic Community (EEC). The EEC created the legal foundation for cooperation with countries in sub-Saharan Africa, the Caribbean and the Pacific Ocean (the ACP states), as well as with the overseas countries and territories (OCT).[3] The Yaoundé I and II Conventions signed in 1963 and 1969 between the Associated African States and Madagascar (AASM) and the EEC were the first steps towards forming a partnership under the Lomé Convention and Cotonou Agreement.

The start of the twenty-first century finds Europe in the role of a key development partner for the Least Developed Countries (LDCs).[4] As the largest donor of Official Development Assistance (ODA), the EU and its Member States provide more than half of the financial support given to LDCs. The EU has special relations with almost all developing countries and

provides them with assistance in a multitude of areas. European development cooperation represents a fortiori one of the pillars of the external relations of the Union and guarantees that the needs of developing countries can be met appropriately:

- The EU provides aid to more than 160 countries, regions and organisations throughout the world.
- The EU and its Member States provide more than half of the world's development aid to countries.
- In 2011, the EU granted €53 billion for development aid, of which €12.3 billion was disbursed by the European Commission, making it one of the biggest aid agencies in the world.
- The role of the EU is particularly important in Africa; more than 70% of the aid given to sub-Saharan Africa comes from the Union and its Member States.
- The EU is by far the biggest trading partner for the African continent. In 2010, 38.8% of total imports to Africa originated in Europe. In the same year, 37.9% of exports from Africa went to the EU.

European development work includes cooperation with

- 78 countries in Africa, the Caribbean and the Pacific within the framework of the Cotonou Agreement;
- developing countries and regional organisations in Asia and Latin America; and
- countries bordering the south and east of the Mediterranean.

Additionally, the EU provides aid to countries in the Middle East and Central Asian countries of the former Soviet Union, supplies emergency relief

both outside and within its cooperation agreements, and is involved in development projects with non-governmental organisations (NGOs).

Legal framework

Principles of development cooperation: Rome, Maastricht, Nice

The Treaty of Rome granted associated status to 31 OCTs. The aim of this affiliation of former colonies was to promote economic and social development, creating close economic ties with countries and regions in receipt of assistance. Additionally, the EEC Treaty (Arts. 131 and 136) created the European Development Fund (EDF). The EDF guaranteed technical and financial support to former colonies in Africa, as well as unilateral tariff preferences (Art. 184) to promote their development.[5]

It was not until the Maastricht Treaty of 1993 (title XX, Arts. 177 to 181), that the area of development cooperation was described as an independent policy area and established firmly at the Community level. This was followed by the Treaty of Nice in 2001, which pursued the provisions with Article 177, standardising the Community's priority areas for development cooperation. Furthermore, the Treaty of Nice included a new chapter on Economic, Financial and Technical Co-operation with Third Countries (Art. 181a), which was mainly intended to introduce the potential for separate aid arrangements with pre-accession countries and neighbouring countries.

Principles of development cooperation in the Lisbon Treaty

The Treaty of Lisbon partly incorporates the provisions of the Treaty of Nice in Article 208, subsequently creating the Treaty on the Functioning of the European Union (TFEU).[6] With the implementation of the latter treaty, the EU attained its own legal personality, thereby replacing the European Community.

Article 208 of the TFEU underlines that the reduction and, in the long-term the eradication, of poverty is the primary objective of the Union's policy on development cooperation. This objective cannot be seen in isolation; it must be viewed in the context of the principles and objectives of the external actions of the Union as outlined in Article 21 of the Treaty on European Union (TEU). According to the TEU, the Union will base its international actions on the founding principles of its own creation.[7] In accordance with the Charter of the United Nations, this includes democracy; rule of law; the universal validity and indivisibility of human rights and fundamental freedoms; and respect for human dignity, equality and solidarity; as well as respect for international law.

With a view to upholding the commitments of the 2005 Paris Declaration on Aid Effectiveness, Article 4 of the TFEU stipulates that EU development policy should strive to complement the corresponding policies of the Member States. This is reiterated by Article 210 of the TFEU, which asks Member States and the EU to coordinate their development policies and gives the Commission the right to take the initiative in promoting this principle.

The Lisbon Treaty reinforced the EU commitment of promoting policy coherence for development (PCD). Article 208 of the TFEU states that the EU shall take account of the objectives of development cooperation, notably the reduction or eradication of poverty, when implementing non-aid policies that are likely to have an impact on developing countries. It is interesting to note that in no other EU policy area where the EU and Member States enjoy a shared competence does such a broad-based coherence exist.

A vision of European development cooperation: the European Consensus

In December 2005 the Council, the European Parliament and the Commission took the unprecedented step of agreeing to a joint and

comprehensive policy statement on the EU's development policy. This European Consensus on Development[8] commits the Union to pursuing development cooperation, be it jointly at EU level or individually at Member State level. In essence, the Consensus expresses four new commitments:

- mobilising more aid, for example by bringing EU ODA up to 0.7% of gross national income by 2015;
- providing faster and more effective aid in line with the Paris Declaration principles on promoting ownership, alignment, harmonisation, mutual accountability and managing for results;
- improving the coherence of EU policies that have an impact on developing countries; and
- giving priority to the poorest and least developed countries, notably those in Sub-Saharan Africa.

Whereas the first part of the European Consensus deals with a common set of values, principles, objectives and means, the second part relates to the Commission's role in spearheading the further development and implementation of the joint policy. Specific attention is given to its role in facilitating coordination and harmonisation at EU level and promoting policy coherence, especially in areas falling under EU competence, and which have far-reaching effects on environmental, economic, political and social conditions in developing countries.[9] PCD aims to maximise the contribution of non-aid policies to development while minimising their potentially negative effects. Moreover, the Commission's role as the implementing body for Community development assistance, accounting for about a fifth of overall EU aid annually, is underlined. The debate on aid effectiveness is, however, not only concerned with the Commission's performance as an implementing donor but also with the collective donor performance of all EU Member States; the Treaties give the coordinating role in this to the Commission.

While the European Consensus is still widely viewed as an invaluable reference point for all development actors more than five years after its adoption, an update may be necessary to reflect the evolution of the broader development agenda, which goes beyond traditional aid, as well as the new approaches to global challenges and their interactions with development policy.

Implementation and financing of the European development policy

The EU has set up numerous programmes to implement its objectives, as well as to increase cooperation between players in the EU and partner countries. For the financing period 2007–13, a number of geographical and horizontal instruments in European development cooperation exist. Assistance may also be provided through the Centre for the Development of Enterprise (CDE) and ProInvest.

Geographical instruments of European development cooperation

Instrument for Pre-accession Aid[10]

The Instrument for Pre-accession Aid (IPA) replaces the instruments that were used until 2006: the PHARE[11] programme; the Instrument for Structural Policies for Pre-Accession (ISPA); the Special Accession Programme for Agriculture and Regional Development (SAPARD); pre-accession aid for Turkey; and the Community Assistance for Reconstruction and Stabilisation (CARDS). The IPA helps candidates and potential applicant countries to improve their social and economic development, and to prepare themselves for the period after accession. For the financing period 2007–13, €11.5 billion has been allocated.

European Neighbourhood and Partnership Instrument[12]

As part of the reform of the external aid architecture, the MEDA[13] and TACIS[14] programmes were replaced by a single instrument in January 2007:

the European Neighbourhood and Partnership Instrument (ENPI). The ENPI concerns the immediate neighbours of the EU in south-east Europe and the Mediterranean region. This instrument is geared towards fostering sustainable development and alignment with EU policies and standards, including the promotion of democracy and human rights, in partner countries.

Around €12 billion of EU funds have been provided to support reforms in partner countries for the current financing period (2007–13), representing an effective increase of 32% from the last financing period.

Development Cooperation Instrument[15]

Development cooperation in the EU used to be governed by a large number of separate geographical and thematic instruments. The development cooperation instrument (DCI) has streamlined the previous framework for the EU's development cooperation by merging the various geographical and thematic instruments into one, resulting in a considerable trans-regional and thematic expansion.

In the area of geographical cooperation, the DCI covers Central Asia, the Middle East, Latin America and South Africa. It also incorporates a number of trans-regional programmes, notably, 'food security'; 'environmental protection and sustainable development of natural resources, including energy'; 'investing in people'; 'non-state actors and local authorities in development'; 'migration and asylum policy'; and 'restructuring of sugar production'. The budget for implementing the DCI over the 2007–13 period was set at €16.897 billion, with €10.057 billion for geographic programmes, €5.596 billion for thematic programmes and €1.244 billion for ACP Sugar Protocol countries.

European Development Fund

The EDF is the main instrument for providing EU aid for development cooperation in the ACP states and the OCT. The EDF does not come under

the EU budget but is financed directly by the Member States, through specific financial and administrative management procedures. The EDF was first programmed and disbursed under the Yaoundé and Lomé Conventions, and since the 1990s under the Cotonou Agreement. Agreements under the EDF are designed to promote the economic, social and cultural development of the ACP states; to contribute to peace, security and regional integration; and to promote a stable and democratic political environment.

At the proposal of the European Commission, EDF budgets are concluded through internal agreements between Member States and the Commission. These run for a period of six to seven years. While the Commission is responsible for managing the EDF,[16] some of the funds are channelled through the European Investment Bank to make use of its competences. This is particularly the case for the provision of loans and guarantees intended to strengthen partner institutions.

The tenth EDF, for 2007–13, has a budget of €22.682 billion. Of this amount, €21.966 billion was allocated to ACP countries, €286 million to the OCT, and €430 million to the Commission to help finance programme planning and EDF implementation.

Horizontal instruments of European development cooperation

In addition to the geographical instruments, there are several horizontal instruments of European external aid. One is the European Instrument for Democracy and Human Rights (EIDHR). The EIDHR supports democracy and human rights in third countries, offering financial support primarily to non-governmental and international organisations. These measures are implemented at a global level as well as within individual regions and countries. For 2007–13 the EIDHR has a budget of €1.104 billion.

Another horizontal instrument is the Instrument for Stability (IfS) which supports EU development policy in third countries affected by conflict or

natural disaster, financing measures both for crisis prevention and crisis response. The objective is to break the erratic stop–go policy cycle brought about by crisis, enabling the pursuit of long-term development objectives.[17] This ties in closely with long-term EU measures for fighting terrorism and organised crime, ensuring the security of international transport and energy networks, as well as efforts to fight epidemics on an international scale. The IfS has a budget of €2.062 billion for 2007–13.

Finally, the Nuclear Safety Co-operation Instrument (NSCI) finances measures to support nuclear safety, radiation protection and the application of safeguards for nuclear materials in third countries. As of 1 January 2007, it replaced the TACIS Nuclear Safety Programme, which had previously covered the safety of nuclear installations in the New Independent States (NIS) created as a result of the break-up of the Soviet Union. The NSCI has a budget of €524 million for 2007–13.

Implementation of development cooperation

Following institutional reforms stemming from the implementation of the Lisbon Treaty, the new Directorate-General for Development and Cooperation (DEVCO) and the Directorate-General for Enlargement (for neighbourhood and pre-accession countries) are responsible for implementing development policy. The creation of DEVCO allows the European Commission to speak with one voice on development policy and cooperation issues, and provides a single contact point for stakeholders both inside and outside the EU. In addition, DEVCO will be the single interlocutor for the European External Action Service (EEAS), as well as for all sectoral Directorate-Generals.

Selected modalities of EU development cooperation

Project aid

The Commission pursues project aid for initiatives not only in the public sector, but also in support of and through civil society and the private sector.

Capacity and institution building are key objectives for project-based aid delivery. Projects are also implemented where conditions do not permit the adoption of a sectoral approach or budget support. Nonetheless, in practice it is often difficult to separate project aid from programme-oriented aid. Often, in addition to specific projects, entire sectors are assisted, such as the natural resources sector, production sectors, economic infrastructures, and services or social infrastructure.

Project aid is managed in a way that guarantees convergence with EU and partner country policy objectives. In line with aid effectiveness principles, projects must support country-owned policies, be sustainable and target realistic objectives.

Budget support

The EU defines budget support as the transfer of financial resources from an external financing agency to the national treasury of a partner country following respect by the latter of the agreed conditions for payment. The financing is then part of a partner country's global resources to be used in accordance with its public financial management rules, increasing the resources available to implement its budget according to its own procedures. Over the period 2003–9, about 25% of the resources available for partner countries' national programmes were allocated to this instrument, with this increasing over time and notably so in the tenth EDF.

Understanding the definition of budget support is just the start. There are different varieties of budget support, including general budget support and sectoral budget support. While both represent a transfer to the national treasury of a partner country, the former supports a national development or reform strategy and the latter supports a sectoral policy or strategy and can address in a more focused manner the specific needs of a particular sector or reform. These different objectives are reflected in the conditions and dialogue between the Commission and its partner countries.

The European Commission holds that budget support is one of the most effective instruments for encouraging partner countries to implement their strategies to reduce poverty, bring about macroeconomic stabilisation and improve public financial management. Furthermore, it enables donors to promote good governance by supporting the partner country's institutions, especially in the area of public finance. The following are some benefits of budget support:

- increased ownership: budget support is based on the premise that supporting a partner country's policies and strategies through the budget makes local authorities more accountable;

- a more stable macroeconomic framework: since budget support provides resources to the budget and the balance of payments, it effectively assists a country in establishing a stability-oriented macroeconomic framework;

- a better framework for public policy and public expenditure: by integrating donor support into the budget, budget support offers the potential to improve the framework for public policy and public expenditure;

- higher potential for overall impact: by focusing on the overall picture, budget support avoids creating 'islands of perfection' while leaving fundamental and systemic problems unaddressed;

- increased coherence: budget support has the potential to achieve a more coherent mix between sectors, between capital and recurrent spending, and within recurrent spending between salaries and non-salary costs;

- lower transaction costs: by eliminating project management units and promoting common reporting obligations the transaction costs of delivering aid as budget support are potentially lower than in other forms of aid;

- greater harmonisation of donor practices and alignment with government procedures: by focusing support on national or sectoral policies and strategies, budget support creates incentives for harmonisation among donors;

- improved domestic accountability: since budget support funds flow through government accounts and budgets, they are subject to parliamentary scrutiny as well as national oversight bodies and governments can be held accountable for their use;

- improved capacity development: budget support does not rely on the use of parallel and often costly outside management structures with their own staffing arrangements and management procedures; and

- increased efficiency and sustainability: the fact that budget support is integrated into the public financial management procedures of a country increases the likelihood of aid having a lasting effect.

Budget support also carries clear benefits for the EU and its Member States:

- Budget support is part of an inevitable trend towards more effective aid, channelled through national institutions that shoulder their responsibilities.

- Budget support gives donors the right to assess a partner country's entire budget and discuss it with the partner. As a result, donors have an overall view of revenue and planned expenditure and can give their opinion on the budget and the various stages in domestic budget procedures.

However, questions from a range of stakeholders such as the European and national parliaments, the European Court of Auditors and civil society remain about the quality, value for money and impact of budget support.

Furthermore there are demands for a coordinated EU approach towards budget support. The European Commission acknowledges that although budget support is one of the best methods for development cooperation, it is also the most demanding for partner countries and donors alike. In order to address these challenges, the European Commission held a public consultation in 2010[18] and published, in October 2011, a communication on the future of budget support.[19] It proposes an EU approach to make budget support more effective and efficient in delivering development results by strengthening the contractual partnerships with developing countries. Concretely, it provides for three types of budget support contracts with third countries in the future:

- 'Good Governance and Development Contracts' will be set up to provide general budget support where the partner country can demonstrate a commitment to fundamental values. The EU will put more emphasis on human rights, democracy and the rule of law through a focus on dialogue with partner countries, creating incentives for reform and asking countries to commit to fundamental values.

- The promotion of sector service delivery will go through 'Sector Reform Contracts'. Sectoral budget support remains a useful tool even when the conditions do not exist to permit the use of a Good Governance and Development Contract.

- Budget support will be used in fragile countries on a case by case basis to ensure vital state functions and support the transition via 'State Building Contracts'.

Millennium Development Goals Contract

One of the lessons the European Commission has learned from traditional budget support is that its effectiveness could be further enhanced if it was more long-term and more predictable. This would help countries to

embark on the kind of spending programmes needed to achieve the Millennium Development Goals (MDGs). This is especially true with respect to the social sectors that have substantial long-term recurrent cost requirements, where returns on investments may only materialise over a longer period.

As a result, the European Commission developed an additional form of budget support, the MDG Contract, which seeks to respond to these calls for more predictability, with the following key features:

- a six-year time frame;
- a minimum level of support which would be virtually guaranteed each year, except in the case of an unambiguous breach of eligibility;
- annual monitoring with a strong focus on results;
- performance assessed in a multi-annual framework that takes both previous performance and future prospects into account;
- an initial focus on the strongest performers; and
- a contract, with firm obligations set out in signed financial agreements.

As it stands, the Commission and the Member States have identified eight countries that qualify for the MDG Contract: Burkina Faso, Ghana, Mali, Mozambique, Rwanda, Tanzania, Uganda and Zambia.

Aid for non-governmental organisations

The Commission makes direct financial contributions in the form of grants to projects or organisations which further the interests of the EU or contribute to the implementation of an EU programme or policy. The EU

supports the development policy work of NGOs by concluding co-financed service agreements with them. While supporting NGOs has increased in importance since the start of the 1990s, overall expenditure has remained relatively constant.

Support for the HIPC Initiative

Launched at the instigation of the G7 countries,[20] the Heavily Indebted Poor Countries (HIPC) Initiative of the World Bank and International Monetary Fund (IMF) seeks to reduce poverty by helping countries to break out of the debt cycle, freeing up new funds for investments and savings. The EU contributes to the HIPC Initiative in two ways, as a creditor providing debt relief to eligible countries and as a donor supporting the World Bank's HIPC trust fund.[21]

Participating countries are subject to binding conditions, which include good governance, transparency of government operations, a prudent macro-economic policy and extensive measures to reduce poverty. Indeed, only if the partner countries actively pursue poverty reduction and tackle structural weaknesses in their economies can debt relief be sustainable.

Compensatory financing to mitigate external shocks: the FLEX and Vulnerability-FLEX mechanisms for ACP countries and the food facility

The instability of export earnings is a serious impediment to development in ACP countries, hindering progress towards joint development objectives. As a result, in accordance with paragraph 1 of Article 68 of the Cotonou Agreement, a system of additional assistance (FLEX) was set up to limit the adverse effects of unstable export earnings. In 2009–10 the European Commission also channelled €500 million into a new Vulnerability-FLEX mechanism with the intention of providing financial support to the ACP countries most affected by the financial crisis. Vulnerability-FLEX provided counter-cyclical support in the form of grant finance, mostly through budget support, where EU funding was able to close outstanding fiscal financing gaps in close coordination with other

international financial institutions, notably the IMF. It also guaranteed expenditure levels in priority areas, thereby moderating the social costs of the crisis in those countries. Furthermore, in order to respond rapidly to problems caused by the food crisis in developing countries, the EU channelled €1 billion in assistance into a food facility. This operated over a three-year period from 2009–11, bridging the gap between emergency aid and medium- to long-term development aid.

Trade facilitation in the context of trade promotion and regional integration

Economic Partnership Agreements

Economic Partnership Agreements (EPA) are regional trade agreements between the EU and ACP countries which aim to promote regional integration, trade and economic growth in order to reduce poverty. The EPAs are a key element of the Cotonou Agreement of 2000. They were adopted after a major consultation launched in 1996 with a view to making trade a more effective instrument for development than the previous unilateral trade preferences. Being limited by market access, they have not produced the expected growth and have also been declared by World Trade Organization (WTO) panels to be incompatible with WTO legal obligations.

EPAs grant signatory countries fully duty-free and quota-free access to EU markets for an undetermined period, while simultaneously providing ACP states with some protection from sensitive EU imports into their domestic markets. Yet they go beyond conventional free-trade agreements by focusing on development, taking account of the ACP countries' socio-economic strategies and constraints, and covering trade-related issues such as investment, trade facilitation, competition, public procurement and intellectual property that are essential to creating a pro-investment environment. All EPAs include development and assistance provisions to help ACP countries implement the joint agreements and to facilitate regional integration, export promotion, capacity building and institutional strengthening.

The EU's 'Everything But Arms' Initiative

In February 2001, the Council adopted the 'Everything But Arms' initiative,[22] granting duty-free access to imports of all products from LDCs without any quantitative restrictions,[23] except for arms and munitions. The initiative ensures that the special arrangements for LDCs are maintained for an unlimited period of time, freeing them from the periodic renewal of the Community's scheme of generalised preferences.

Humanitarian aid

With the Community aid managed by the European Commission and the bilateral aid offered by Member States, the European Union is collectively the world's leading humanitarian donor. In 2006 it contributed over €2 billion, or more than 40% of total international humanitarian assistance. Food aid, being a humanitarian tool, is also managed by the Directorate-General for Humanitarian Aid and Civil Protection (ECHO) under the Instrument for Humanitarian Aid. Since successful provision of humanitarian aid can be achieved only through close cooperation between all participants at the international level, the respective residents of the Commission, the European Parliament and the Council of the EU signed the 'European Consensus on Humanitarian Aid' in December 2007. This laid down the common values and principles underlying the humanitarian action of the EU in order to reinforce the complementarity between Member States' and Community humanitarian action, and to enhance the effectiveness of the EU humanitarian aid effort.

Since 1992, ECHO, through its partners, has funded humanitarian aid in crisis zones in more than 85 countries. Its grants cover emergency aid, food aid, and aid to refugees and displaced persons worth around €700 million a year.

Concluding remarks and outlook

The objectives and values that the EU pursues internationally are inherently linked to its internal dynamics. The EU's foreign policy objectives and the way in which they are pursued are key elements of its international identity, indicating what the EU considers to be important.[24]

Representing more than half of ODA worldwide, Europe is a global player in advancing sustainable development. With respect to humanitarian aid, the EU is the world's single largest spender of general humanitarian aid, with a budget of €1 billion a year. Indeed, European development cooperation has evolved into a fundamental pillar of EU external policy. It needs to go hand in hand with policies in other areas, namely trade, foreign policy and security policy, but also agriculture, environment, energy, transport and justice. Only through a comprehensive approach will it be possible to sustainably address the shared global challenges. Over the last decade, EU Member States have started to develop a 'common vision' and to increase the coordination of policies and actions in line with their common pledge to increase ODA, achieve the MDGs and implement the Paris Declaration on Aid Effectiveness.

Despite this shared vision, EU development policy is at a crossroads. Key international challenges need to be addressed including the effects of the financial crisis,[25] climate change and increasing natural resource scarcity, access to and supply of energy, food insecurity, international migration, global pandemics, regional and intra-state conflicts, and international terrorism. This requires a profound rethinking of how development policy can best contribute to tackling these global problems and protecting global public goods. The international landscape is also changing. New global players (such as Brazil, Russia, India and China) are emerging as donors with clearly articulated long-term strategic interests, both economic and political, in developing country regions. Simultaneously, traditional donors are being heavily affected by budget austerity at home and are increasingly challenged by those who question the effectiveness of traditional aid. Finally, the Lisbon

Treaty has created a new institutional architecture for conducting foreign and security policy, *inter alia* through the creation of the position of the high representative and the EEAS.

In this context, the EU, together with other traditional donors, has to demonstrate that development aid leads to tangible and measurable outcomes that improve the standard of living for the poor in developing countries. The EU also has to focus on its own added value by establishing a more systematic—that is, sectoral and geographic—division of labour, including more joint programming, with its Member States. Reducing and eventually eradicating poverty is in the enlightened self-interest of the EU; security, justice, growth and job creation in the EU is intrinsically linked to peaceful, stable and prosperous partner countries, especially in those regions close to Europe such as the Mediterranean, Central Asia and sub-Saharan Africa.

In response to these challenges, the European Commission published its vision for the future of development cooperation in October 2011: the Agenda for Change. The communication states that EU aid should be directed where it is needed most and where it can have the greatest impact.[26] This includes concentrating on the poorest countries, and on a limited number of sectors per country, where the EU can make the biggest difference. Future EU spending will also concentrate on sectors which are key for long-term and inclusive growth (such as agriculture, energy, health, education and social protection).

In order to generate more resources, the EU will explore innovative ways of financing development, such as the blending of grants and loans. The Commission will also encourage the EU and its Member States to jointly prepare strategies and programmes and better divide labour amongst themselves in order to increase aid effectiveness.[27]

The EU plays a multifaceted role in developing countries. It implements development aid, initiates the coordination of its own cooperation actions and those undertaken by its Member States, makes development policy, and acts as an economic and trade partner and a conceiver and implementer of

non-aid policies. These policies are subject to the EU's reinforced commitment to policy coherence for development in areas such as migration, energy, the environment, agriculture, taxation, financial regulation and fisheries. Moreover, the EU is increasingly playing a role in the field of security and defence by making use of its civilian and military assets to support peace-building and peace-making. While these roles are a significant challenge for an actor establishing a new capacity in external action and development cooperation, they provide an enormous opportunity to realise the synergies that a more effective EU could present.

Ultimately, the EU will continue to 'learn by doing' and so establish itself as an international development actor, helping to shape not only its partner countries' futures but also the international environment in which Europe operates. In this respect, successful European development cooperation must make an effective contribution to eradicating poverty while simultaneously pursuing the creation of a just and democratic world order, inspired by the idea of protecting and developing universal, inalienable human rights and freedoms.

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Notes

[1] The development policy of the EU, according to the Lisbon Treaty, does not replace development cooperation by individual Member States, but complements and harmonises it.
[2] Art. 21 of the Treaty on European Union (Lisbon Treaty).
[3] Many of the countries in these regions were colonies of Member States at the time.
[4] Today the EU also carries considerably more political weight than at its inception.
[5] Tariffs on goods exported from associated regions to Member States are not allowed.
[6] The Treaty of Lisbon amends the EU's two core treaties, the Treaty on European Union and the Treaty establishing the European Community. The latter was renamed the Treaty on the Functioning of the European Union. In addition, several protocols and declarations were attached to it.
[7] These include areas it would like to further legitimise through its actions.
[8] Although the Consensus is not legally part of the *acquis communautaire*, it is considered a baseline policy for steering the implementation and evolution of EU development policy.
[9] The EU commitment to PCD is also confirmed in the Treaty of Lisbon in Art. 21 of the TEU, which states that 'the Union shall ensure consistency between the different areas of

its external action and between these and its other policies', as well as in Article 208 of the TFEU, which affirms that 'The Union shall take account of the objectives of development cooperation in the policies that it implements which are likely to affect developing countries.'

[10] Council Regulation (EC) no. 1085/2006 establishing an Instrument for Pre-Accession Assistance (IPA), OJ L210 (17 July 2006), 1.

[11] PHARE originally stood for 'Poland and Hungary: Assistance for Restructuring their Economies' but subsequently also covered the other accession countries and became a programme name in its own right.

[12] European Parliament and Council Regulation (EC) no. 1638/2006 laying down general provisions establishing a European Neighbourhood and Partnership Instrument, OJ L310 (24 October 2006), 1.

[13] The acronym MEDA originally stood for 'Mésures d'accompagnement financières et techniques' but the full title was not commonly used and the acronym became a name in its own right.

[14] The acronym TACIS originally stood for 'Technical Assistance to the Commonwealth of Independent States' but subsequently it became a name in its own right.

[15] European Parliament and Council Regulation (EC) no. 1905/2006 establishing a financing instrument for development cooperation, OJ L378 (18 December 2006), 1.

[16] This is done in collaboration with the EDF committee, on which the Member States are represented.

[17] These objectives include measures to build and maintain peace, and to rebuild the economy, the administration, the justice system and government as well as the social services and the local community.

[18] European Commission, *The Future of EU Budget Support to Third Countries*, Green Paper, COM(2010) 586 final (19 October 2010).

[19] European Commission, *The Future of Budget Support to Third Countries,* COM(2011) 638 final (13 October 2011).

[20] The G7 is an international finance group consisting of the finance ministers from seven industrialised nations: the US, the UK, France, Germany, Italy, Canada and Japan.

[21] The biggest share of the EU's support to the HIPC Initiative goes to ACP countries. So far, more than €1.6 billion has been pledged, €680 million in relief on its own claims and €934 million to the HIPC trust fund.

[22] Council Regulation (EC) no. 416/2001 amending Regulation (EC) No 2820/98 applying a multiannual scheme of generalised tariff preferences for the period 1 July 1999 to 31 December 2001 so as to extend duty-free access without any quantitative restrictions to products originating in the least developed countries, OJ L60 (28 February 2001), 1

[23] Bananas, sugar and rice were excluded for a limited period.

[24] The EU's foreign policy objectives include encouraging regional cooperation and integration; promoting human rights, democracy and good governance; preventing violent conflict and preserving peace; fighting international crime and terrorism; and improving social and economic conditions in less developed countries.

[25] The economic crisis has slowed down progress towards the MDGs, particularly in low-growth and fragile countries. This has been exacerbated by repeated food price spikes and recent regional disasters such as droughts in the Horn of Africa and the Sahel. (For more information see World Bank, *Global Monitoring Report 2012*, *Food Prices, Nutrition, and*

the Millennium Development Goals, accessed at http://econ.worldbank.org/WBSITE/EXTERNAL/EXTDEC/EXTDECPROSPECTS/0,,contentMDK:23148901~pagePK:64165401~piPK:64165026~theSitePK:476883,00.html on 19 March 2013.

[26] European Commission, *Increasing the Impact of EU Development Policy: An Agenda a for Change*, COM(2011) 637 final (13 October 2011).

[27] The proposals for the EU's external instruments of the Multiannual Financial Framework 2014–2020, which the Commission presented in December 2011, support the new approach of the Agenda for Change.

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The European Union affects our daily lives. National governments implement regulations and laws which have been made at the EU level. The EU removes barriers between Member States, and we all profit from the freedom of movement of people and services in the EU. However, it is not always clear how these decisions are made, what policies are in place or the consequences these have for citizens and the EU as a whole. With much ongoing debate about reforming Europe, it is now more important than ever to know more about EU policies.

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