THE REFORM OF THE STRUCTURAL FUNDS:
A REVIEW OF THE RECENT DEBATE

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This paper has been prepared for discussion at the twenty-third meeting of the Sponsors of the European Policies Research Centre to be held at Ross Priory, Loch Lomondside on 7 and 8 October 2002.

September 2002

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1. INTRODUCTION

Over the past year, the debate on the reform of the Structural Funds has intensified. Although the current financial planning period still has more than four years to run, and the start of formal negotiations is at least 18 months away, European institutions, Member States and regional and sectoral interests have begun to engage seriously with the issues. In particular, the debate is moving out of the realms of academic research on the costs and benefits of enlargement, and the scenario for reform, to involve political and administrative discussion of specific reform options and priorities.

The following paper examines recent developments in the reform debate, updating the report to Sponsors produced in September 2001[1]. It begins with a brief overview of the key issues and timetable of the reform debate before looking in more detail at the different perspectives of the current Member States and the Candidate Countries. These national positions are expressed in political statements and official papers and the focus is primarily on the views of national government authorities, since the views of the wide range of other bodies has already been well documented in Commission publications. Lastly, the paper considers some of the specific proposals for the reform of the Funds and identifies issues for discussion

2. PARAMETERS OF THE DEBATE

2.1 Key issues

The starting point for the debate is the impact of enlargement on regional disparities in the EU. As described in detail in the Second Cohesion Report and the First Progress Report, accession of ten Candidate Countries (CCs) would lead to a fall of 13 percent in the average level of GDP per head in an EU of 25 countries. Convergence in per capita GDP between the CCs and the EU-15 is a long-term process; recent figures suggest that it could take 25-30 years for many of the CCs to reach even 75 percent of the EU-15 average. There are clearly major challenges with respect to investment in public capital, levels of entrepreneurship and SME activity, skills deficits, technological obsolescence, environmental legacies, the efficiency of market economic institutions and the need to modernise public administration.

The implications for EU regional policy stem from the fact that several of the new Member States have a per capita GDP of less than half the EU average. The statistical effect of lowering the average EU GDP per capita figure will be to shift several of the current Objective 1 regions above the 75 percent threshold. According to the Commission's analysis, 37 million people are contained in the regions currently eligible under Objective 1 which after enlargement would be above the 75 percent threshold. About one-third of this total would be above the 75 percent threshold

[1] Bachtler J (2001) *EU Regional Policy in an Enlarged Union: A Review of the Debate*, Report to Sponsors, European Policies Research Centre, University of Strathclyde, Glasgow.

irrespective of enlargement by virtue of relative regional economic growth, but the remainder would be above the threshold due to the 'statistical effect'.

In resolving the competing needs of the current and future poorer regions of the EU, it appears unlikely that there will be a significant increase in the financial resources available for EU regional policy. The Commission regards a target of 0.45 percent of the EU's GDP as a "minimum below which the credibility of future cohesion policy would be called into question",[2] but across the EU there are widely differing views from those who advocate a substantial increase in resources for EU regional policy to those who regard 0.45 percent as a ceiling and would prefer cutbacks in expenditure.

While there is broad consensus on the need for EU regional policy to focus on the least developed regions, there is no agreement as yet on how to define these areas. The Commission has suggested four ways in which the eligibility of lagging regions might be undertaken:[3]

1. application of the present threshold of 75 percent irrespective of the number of countries joining the EU;

2. application of the present threshold of 75 percent but where all regions above this threshold but currently eligible under Objective 1 should receive temporary phasing-out support;

3. setting of a GDP per head threshold higher than 75 percent of the average at a level which would reduce or eliminate the statistical effect; and

4. fixing of two thresholds of eligibility, one for the regions in EU-15 and one for the Candidate Countries.

Looking beyond the lagging regions, there is also no consensus as to whether and how EU regional policy should provide support for other development priorities. The Commission has identified ten thematic and territorial priorities where, it argues, the Community has a justifiable role: industrial areas undergoing conversion; rural areas undergoing conversion; urban areas in difficulty; areas facing specific geographical or demographic handicaps; cross-border, transnational and interregional co-operation; social inclusion; equality of opportunity; the new economy and knowledge society; and more and better jobs.

Apart from financial allocations, the debate has been concerned with the value added of EU intervention. This encompasses a redefinition of roles and the distribution of tasks between the Commission and Member States, as well as the need for simplification of the processes for managing, delivering and controlling the Structural Funds.

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[2] CEC (2001b) *Unity, solidarity, diversity for Europe, its people and territory*, Special Report in Economic and Social Cohesion, Commission of the European Communities, Brussels.

[3] CEC (2001a) Commission summary of the Second European Cohesion Forum, Brussels.

2.2 Timetable

The reform debate was effectively launched by the publication of the Second Cohesion Report (January 2001) and the Second European Cohesion Forum (May 2001), both organised by the European Commission, and the Informal Meeting of Regional Policy Ministers (June 2001) organised under the Belgian Presidency in Namur. Since then, the Commission has published its first 'Progress Report'[4] on economic and social cohesion in an enlarged European Union and has initiated a series of seminars on the future priorities for the funds, beginning with a seminar on 'defining Community value added' (May 2002). It has also convened a 'groupe de prospective' to examine territorial and horizontal priorities for the Funds in more detail.

Member States have been engaged in internal consultations among governmental departments and with regional and sectoral interest groups, to varying degrees, as well as commissioning further research studies, to lay the groundwork for developing formal negotiating positions. There has also been some multilateral debate on reform in the Working Party on Structural Measures (under the General Affairs Council) and COREPER, most recently under the Spanish Presidency, where preliminary responses to the First Progress Report were considered by Member State officials.

Looking forward, the next 'milestone' will be the publication of the Second Progress Report by the Commission in January 2003, updating the analysis of economic and social cohesion and the evolution of disparities in an EU-25/27. An Informal Meeting of Regional Policy Ministers under the Greek Presidency has also been mooted, but the key period in the debate is expected to be late 2003/early 2004 with the publication of the Third Cohesion Report and subsequent Commission proposals for the proposed content of EU regional policy after 2006 (see box).

Notional timetable for the reform debate and negotiations

January 2003	Second Progress Report
November 2003	Third Cohesion Report
January 2004	Third Cohesion Forum
Spring 2004	EC adoption of Agenda 2007 proposals
Summer 2004	Preparation of new Structural Fund legislative texts
Late 2005/early 2006	Adoption of new Structural Fund legislation by Council
2006	Negotiation of new Structural Fund programmes
2007	Launch of new Structural Fund programmes

The timetable for negotiating and agreeing a reform of the Structural Funds is, however, subject to several important caveats. First, despite recent doubts about the enlargement timetable, the EU is still working towards admitting up to ten new Member States over the 2004-06 period which will significantly change the political

[4] CEC (2002) *First Progress Report on Economic and Social Cohesion*, Commission Communication, COM (2002) 46 final, Brussels.

dynamics of the European institutions and the negotiation process. However, before enlargement takes place there is the potential for politics within Member States to delay the accession process, as exemplified by the debate on Ireland over the ratification of the Nice Treaty. The same applies to the Candidate Countries; for example, a Eurobarometer survey in the Baltic states in March 2002 found that only Lithuania could be sure of a referendum majority in favour of EU membership.

Second, a new Commission will be appointed midway through the process which on the one hand may inhibit the current Commission from 'binding' its successor with detailed proposals, and on the other hand will introduce a delay while the new Commission settles into office. A new European Parliament will also be elected in June 2004.

Third, the reform of the Structural Funds cannot be seen in isolation. Of potentially greater importance for several Member States is the reform of the Common Agricultural Policy and its financial implications. Also significant is the debate about the future of State aids policy in an enlarged EU, the implications for national regional aid and the future relationship between the spatial coverage of EU and national regional policies[5]. There are also other EU policy issues that have a bearing on the reform debate, notably: the discussion about future governance arrangements for the EU, and the allocation of responsibilities between European, national and sub-national levels; the further development of the Lisbon agenda concerning European competitiveness; adaptation to the single currency, and specifically any modification of the Maastricht criteria; and the European justice and security agenda, with particular reference to immigration, the integration of ethnic minorities and the approach to external borders.

Lastly, even within the parameters of the Structural Fund reform debate, there are difficult issues to be addressed. These include the overall budgetary allocations between the Candidate Countries, the current Objective 1 recipients and other priorities and areas; the possibility of a redefinition of the respective roles of the Commission, Member States and sub-national authorities in implementing the Funds; and the need to simplify the management and administration of the Funds.

3. MEMBER STATE VIEWS

Among EU Member States, there is intensive discussion about the reform of the Structural Funds, but for the most part at a general level. Most countries are taking a reactive approach at present, waiting for or responding to proposals and ideas from the Commission and other Member States. No country has yet taken a definitive policy position, a situation that is likely to continue until the Commission puts forward concrete proposals. Also, the debate often needs to be viewed within the wider context of discussion about the 'future of Europe on the governance'.

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[5] Wishlade F (2002) *Competition policy and regional aid: a highly-charged agenda*, Report to Sponsors, European Policies Research Centre, University of Strathclyde, Glasgow.

In this context, the common ground among EU countries appears to be limited to three broad issues:

- EU regional policy is important and necessary for solidarity between richer and poorer parts of the EU;
- the less-developed regions should remain the main priority of future regional policy;
- the administration of EU regional policy needs to be simplified.

Although the debate is still in its early stages, a divide is already becoming apparent between Member States. On the one hand, there are Member States whose main objective appears to be rationalisation of EU regional policy (eg. Germany, the Netherlands, Austria, Sweden, UK), particularly with respect to the cost and administration of the Funds. On the other hand there are Member States (eg. Spain, Portugal, Greece, Italy) which are keen on the further development of EU regional policy, and who regard the Second Cohesion Forum and First Progress Report as setting the terms of the debate about future scenarios. Differences are evident not just in terms of the objectives of Member States to the reform of EU regional policy but also in their attitude to the value of the Funds. For example, it has been argued that, whereas some countries (such as France) are more likely to emphasis the positive aspects of the Structural Funds, the German approach has been to emphasise the inefficiencies and to see the challenge of enlargement as an additional reason to undertake a comprehensive reform as quickly as possible[6].

The following sections examine the stated views of individual Member States in more detail, dividing countries into three broad groups. It is important to note that this categorisation is merely for the purposes of discussion; in practice, the spread of views is more complex, and not mutually exclusive.

3.1 MS perspectives: Rationalisation of EU regional policy

Under this first heading is a group of countries generally opposed to an increase in the EU budget for Structural Funds (eg. Germany, Austria, Netherlands, Sweden, UK). They favour the 'renationalisation' of EU regional policy, which - at it most extreme - would involve a complete cessation of Structural Funds in the richer EU Member States or would involve a simple budget transfer of EU resources to part-fund policies and priorities determined by the Member State. Among these countries, there is considerable support for the view that the EU should only intervene in relatively poor Member States unable to address these problems themselves; outside these areas, EU regional support should focus on actions with a 'real' Community added value such as Interreg. Failing that, post-2006 EU regional policy in the richer countries would transfer more responsibilities for implementation to the Member State level. Several

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[6] Arnaud J-L and Guder U (2002) *Welche Perspektive für die Strukturfonds und die Kohäsionspolitik?* Report on the Seminar of the Stiftung Wissenschaft und Politik und Notre Europe, supported by the French Ministry for Foreign Affairs, 31 January – 1 February 2002, Paris.

of these countries are also vocal in advocating a simplification of the current implementation system.

As the largest EU country and most important contributor to the EU budget, the view of ***Germany*** is of particular significance. The context for the German position is the internal debate about European policy, in particular the division of responsibilities between EU and national levels. In the run-up to the recent elections, both major political parties referred to the transfer of competences back from the EU, allowing Member States more flexibility in operating their own regional policies. Some west German *Länder* politicians (North-Rhine Westphalia, Bayern) have made speeches calling for fundamental reform. For example[7]: "The German Länder have hardly any leeway any more in forming regional policy….We want to regain lost freedom to act on our own initiative and using our own money". The eastern German *Länder* are less keen on 'renationalisation' of EU regional policy, fearing a loss of resources[8]. For the *Länder* governments, in general, the negotiating issues are associated with a reorganisation of national financial transfer systems as well as a simplification of bureaucracy for Structural Funds and more flexibility for operating regional aid.

Specifically with respect to Structural Funds, the German position is that it strongly supports a cohesion policy in the interests of European solidarity, but that EU enlargement should not lead to an increase in spending on EU regional and agricultural policies, and a fundamental reform of EU regional policy is necessary on efficiency grounds. A future EU regional policy must be designed to respect principles of fairness, solidarity, efficiency and financial viability.

Among the recent government statements on the issue, the German Chancellor, Gerhard Schröder, reporting to the German Parliament on the Barcelona Summit in March 2002, said that "Germany, as the country that finances 25 percent of the EU, wants Agenda 2000 to continue being the financial basis for the distribution of aid following enlargement". Furthermore, those "who until now have been the sole recipients" of EU aid would need to show "a bit of solidarity" as neither agricultural aid nor the Structural Funds could be increased.[9]

The main official statement is a speech by the State-Secretary in the Finance Ministry, Koch-Weser, in October 2001[10]:

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[7] Speech given by Wolfgang Clement, Minister President of North Rhine Westphalia *"Shaping – not administering – a new Europe – Allocation of responsibilities within the European Union after Nice"* to the 'Forum Constitutionis Europae' of the Walter Hallstein-Institute for European Constitutional law of Humboldt University, Berlin, 12 February 2001.

[8] Ost-Länder bangen um Förderung, *Handelsblatt*, 22 May 2001.

[9] Regierungserklärung durch den Bundeskanzler zu den Ergebnissen des Europäischen Rates in Barcelona am 15./16. März 2002, Deutscher Bundestag, Berlin.

[10] Speech by Mr Koch-Weser *Einige grundsätzliche Überlegungen zur Ausgestaltung der EU-Strukturpolitik in einer erweiterten Europäischen Union,* Rede anlässlich der Konferenz "10 Jahre Europäische Strukturpolitik in Ostdeutschland – Bilanz und Perspektiven, 17/18 October 2001, Magdeburg.

- "EU cohesion policy has been one of the most successful EU policies and should remain so, but those Member States that have benefited for many years should now show solidarity with the poorer countries. EU aid is meant to be time-limited, a point which is not sufficiently evident in the debate.

- Member States are themselves primarily responsible for addressing internal disparities. Each Member State should demonstrate that they are making sufficient efforts themselves before considering EU aid.

- EU cohesion policy must adapt to financial constraints. The current maximum limit of the EU budget should be significantly underspent even after enlargement. There is a need to identify priorities for future aid and areas where further aid is unnecessary.

- Additional expenditure for cohesion policy in the Candidate Countries after 2006 should be largely financed by savings in the current Member States (€150 bn for 2007-13).

  i. Savings must be fairly distributed across all current Member States. Comparable regions must be treated in the same way. National prosperity should be taken into account also in the allocations of Objectives 2 and 3.
  ii. There is a need to be clear on the added value of Structural Funds, identifying which aspects have been successful (eg. inter-regional cooperation, SME and information society measures) and which actions could be transferred to national and regional levels.
  iii. It is dangerous to talk in terms of a 'need for aid' (eg. EC discussion of urban areas), which raises unrealistic expectations.
  iv. Not all disadvantaged regions with particular geographical problems or characteristics (eg. islands, mountain areas, sparsely populated areas) should be assisted by the EU.
  v. There should be a stricter application of the subsidiarity principle – in all Member States it must be possible to operate a national regional policy."

As noted above, the German Länder are also involved in the debate. The east German *Länder*, led by Sachsen-Anhalt and Thuringen, have been particularly keen to ensure that the significant level of resources under Objective 1 can be maintained after 2006[11] and that "enlargement is not financed at the expense of the poorest regions in the current EU"[12].

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[11] Ergebnisprotokoll, 26. Regionalkonferenz der Regierungschefs der ostdeutschen Länder, 10 October 2001, Erfurt.

[12] Speech of Werner Ballhausen, State Secretart for European Affairs of Sachsen-Anhalt 'Thesen uber die politischen perspekitven der Kohasionspolitik der Europaischen Union mit Blick auf die Erweiterung', at the European Cohesion Forum, May 2001.

Post-2006 scenarios: the view of the German *Länder*

The German *Länder* have considered different scenarios for the Structural Funds after 2006, based on several criteria: the fiscal impact on the net payment position of Germany as a whole: the fiscal impacts on the *Länder*; the fiscal impact on their economic development budgets; consistency with agricultural policy; subsidiarity; administrative resources; flexibility to operate regional aid; participation in exchange of experience; and the role of the regions in European policymaking. On the basis of these criteria, the *Länder* (with some differences in ranking) stated a preference for the following scenarios:

- The 'status quo' scenario: maintaining Objective 1 eligibility at 75 percent would reduce EU regional policy transfers to Germany, eased by phasing out support, but still retain about half of the current level of transfers to the German regions. Would need rationalised administrative processes.

- The 'status quo plus' scenario: increasing the Objective 1 eligibility threshold above 75 percent would help the German regions adapt to enlargement but have negative impacts on the German net payment position. Widening the Structural Funds in the direction of urban and spatial development would be questionable on subsidiarity grounds.

- The 'net fund scenario': this would be beneficial for the German net payment position but would see an almost total loss of Structural Funds (apart from Community Initiatives, networks etc). Administrative savings would be made, but the *Länder* would need 'compensation' of ca. €2.1 billion.

A meeting of the *Land* economic ministers in May 2002 formulated a common position, as follows (see also box).[13]

- "Regardless of enlargement a fundamental reform of the Structural Funds is necessary in order to achieve real simplification and decentralisation. The *Länder* are critical of the administrative complexity and resources required for implementing the Funds.

- In redefining eligibility for the Funds, the German regions should not be treated less favourably that other comparable regions.

- The EC must promote interventions with clear European added value such as pilot projects, networks, exchange of experience, networking and certain Community initiatives.

- The stated upper limit on transfers of four percent of GDP should be maintained after 2006."

[13] Wirtschaftsministerkonferenz, 2-3 May 2002.

The approach of the German government to the reform of EU regional policy is shared in some important respects in *Austria***,** although there appears to be less of a concern with 'renationalisation' and a strict division of competencies, in the way that it is discussed in Germany, since responsibilities are not precisely allocated to specific levels in Austria. Reports suggest that a uniform governmental position on Structural Funds has yet to be agreed: the foreign ministry appears to support the EC proposals (in the first progress report), while the finance ministry has a more critical position, although it does not go as far as the Dutch proposal (see below).[14]

Among public statements, the (former) Austrian Finance Minister, Karl-Heinz Grasser is said to have agreed that EU enlargement should not require additional resources: "We certainly do not want to increase the 1.27 percent of GDP…it is our preference to pay less [for EU structural and agricultural policies] and to allocate the funds to southern and eastern Europe"[15]. The Chancellor, Wolfgang Schüssel, has also argued for more decentralisation and subsidiarity in the field of regional policy and critically questioned the high administrative costs of organising and controlling the Structural Funds.[16] Although he does not appear to be advocating a radical renationalisation of policy responsibilities, he has supported more flexibility for national responsibility in the field of regional policy.[17] A more detailed consideration of some of the issues from an Austria perspective is provided in the box below[18].

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[14] 'Endspurt im EU-Erweiterungspoker', *Der Standard,* 22 April 2002.

[15] 'EU-Mittel vom Suden in den Osten verlargern', *Der Standard,* 27 November 2001.

[16] Eingangsstatement zur Europarunde by Dr Wolfgang Schüssel, 27 June 2002, Hofburg, Vienna.

[17] Eingangsstatement zur Europarunde by Dr Wolfgang Schüssel, 30 May 2002, Hofburg, Vienna.

[18] Personal paper by Wolf Huber (Federal Chancellery, Austria) *Personal reflections on the 'value added' of Structural Funds interventions outside the Cohesion Countries*, February 2002.

Principles for reforming the Funds: an Austrian viewpoint

In a personal contribution to the debate, Wolf Huber, head of Structural Funds in the Bundeskanzleramt has outlined a series of principles for the reform of the Structural Funds:

- The economic justification for EU cohesion policy is limited to interventions in the cohesion countries, i.e. member states whose GDP lies more or less significantly below the EU average. There can be no direct economic value added (in quantitative terms) if funds are simply recycled among "rich" member states.

- Nevertheless, Structural Funds interventions in "rich" member states do make sense, if properly applied. They must however, and can only be, politically justified by qualitative effects ("political value added"). This does not require high amounts of funds. Structural Funds can be a means to make the benefits of European integration visible to the citizens; and they can be an incentive to stimulate regional policy innovations and to facilitate their political implementation.

- The "value added" of Structural Funds interventions is accompanied (and reduced) by considerable additional bureaucratic burdens. To render a positive "net value added" (in "rich" member states at least in political terms) it is necessary to perform administration and control more efficiently and to reduce bureaucratic burdens to an unavoidable minimum.

- In order to increase the (net) value added of EU Cohesion Policy, a new model of policy making is required. What is required much more is a fundamental reflection on - which forms of intervention are adequate to provide a maximum of (net) value added of EU policies; which management methods are adequate to provide a maximum of economic and political efficiency in the implementation of cohesion policy, especially for innovative approaches.

In the ***Netherlands***, the Dutch Government has been one of the most active Member States in debating the reform of EU structural and agricultural policies. It has commissioned a series of interdepartmental studies on the implications of enlargement for EU structural policy and the CAP and the options for reform. The Dutch Cabinet standpoint on the studies was submitted to the parliament in the following terms[19]:

- "The Cabinet endorse the preference expressed by the IBO working group for the reform variant (cohesion approach) under which a national focus is chosen for the allocation of European resources. In practice, this would mean that the rich member states no longer claim EU resources for structural policy.

- If this cohesion approach does not win sufficient support at the European level, the Cabinet is prepared for a debate about the renationalisation of structural policy in the member states ("shortening the balance sheet").

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[19] *Cabinet Standpoint concerning the Interdepartmental Policy Study (IBO) on "European Structural Policy in the Context of the Enlargement of the EU",* Document to the President of the House of Representatives from the Minister of Foreign Affairs, Minister of Finance and Minister for Foreign Trade, The Hague, 2002.

- Whatever the final outcome… the principle of "fair share" should remain the point of departure….the Dutch financial position in relation to that of current, comparable member states is not allowed to be changed for the worse."

This position was submitted to other Member States in the form of a non-paper and in a response to the Spanish Presidency questionnaire in the Working Group on Structural Measures (GAC). The paper, which has been regarded positively by several other 'net payer' countries, made the following proposals[20]:

- "The current focus on relatively poor regions in a Union of relatively rich member states was an agreed cohesion policy in past periods, but is in our view no longer sustainable.

- A national eligibility criterion, like a percentage of average GDP in the EU, allocates the funds where they are most needed: in the poorest member states. Relatively rich member states are able to address their own regional problems. The member states could then make sure that Structural Funds are allocated in the most effective way.

- Complementary to this national focus of the eligibility criterion is a more national focus of the spending criteria.

- There should be a continuation of policies with truly added (community) value at the European level, both in richer and poorer member states. In our view this only applies to real transnational problems, such as those addressed by the Interreg-initiative."

Finally, the ***United Kingdom*** has not yet made a political contribution to the debate on the reform of the Structural Funds. Over the past two years, the Department of Trade and Industry has been engaged in an internal consultation exercise, mainly involving inter-ministerial discussions with HM Treasury and the Office of the Deputy Prime Minister, as well collecting the views of the Devolved Administrations (in Scotland, Wales, Northern Ireland) and the English regions during a 'roadshow' in April-June 2001. As part of this, the UK's priorities for the Structural Funds were defined in the following terms:

- interventions should support the Lisbon agenda: knowledge economy; competitiveness and innovation; investing in people and combating social exclusion; sustainable economic growth and appropriate macro-economic policies;

- Structural Fund reform should not hinder the enlargement process;

- the outcomes of reform should be fair for the UK relative to the rest of the EU-15 and for the Candidate Countries;

- as a net contributor, it is in the UK's interests to the keep the budget down.

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[20] *Non-paper Dutch position on future Cohesion policy,* IBO Group, The Hague, 25 April 2002.

At the informal council in Namur, the UK placed emphasis on understanding the purpose and added value of the Structural Funds as a principle for the reform of EU regional policy. Subsequently, the DTI has initiated an evaluation process to identify the added value of Structural Funds in the UK with a view to guiding its approach to reform.

3.2 MS perspectives: Retention of current EU regional policy support for lagging regions

A different viewpoint has been expressed by the Cohesion Countries, and some other Member States that consider a continuation of a well-financed EU regional policy, in both the EU-15 and the accession countries, to be important. These countries have mostly rejected the prospect of ‘renationalisation’, as expressed in the Dutch paper, as being incompatible with the Treaty. While supportive of the need for reallocating resources eastwards, and reforming the complex implementation of the Structural and Cohesion Funds, they generally take the view that the Funds should be adequately resourced to enable continued substantial support for the poorer parts of the current EU.

Of particular concern is the ‘statistical effect’ on the eligibility of the less developed regions of the EU and the need for transitional (phasing-out) support for Objective 1 regions that become ineligible in an enlarged EU. Arguing that convergence is an important, long-term objective for the EU, they consider that the achievements of EU regional policy hitherto in the Cohesion Countries could be jeopardised by a reduction in support from the Funds.

Spain was one of the earliest countries to voice a political position on the reform of the Structural Funds along these lines. In the so-called ‘Aznar Memorandum’, the Spanish Prime Minister made the following attempt to link Structural Fund reform with progress on the enlargement talks during the first half of 2001[21]. The memorandum recognised the effectiveness of EU regional policy in reducing the development gap between Spain and the rest of the EU but notes the persistence of regional disparities and the ‘statistical effect’ of enlargement on indicators of relative prosperity.

- “Spain fully shares the Commission’s assessment that its financial endowment will possibly require a greater volume of resources insofar as with enlargement not only will the number of Member States increase - and consequently the amount of potential beneficiaries - but also regional disparities.

- However, a problem of loss of resources from structural action arises as a result of the participation of new Member States in this policy, and due to the application of the current distribution and eligibility criteria given the levels of income per head.

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[21] *Regional Policy and Enlargement*, Memorandum by the Spanish Government to the European Commission.

- There would therefore be an artificial acceleration of the economic convergence process. This…would not, in fact, be a real convergence. The situation would affect several Member States and Spain considers that it must be duly taken into account.

- There are several alternatives to minimise or even neutralise this effect produced by the enlargement on the future eligibility of current Member States and their regions. Spain considers that it will be necessary to find a solution to this problem in the framework of the enlargement negotiations."

At a political level, ***Portugal*** has also stressed the importance of maintaining receipts to the current cohesion countries and highlighting the positive impacts of the Structural Funds. Speaking at the European Cohesion Forum, the Portuguese Minister for Planning, Elisa Ferreira, stated[22]:

- "A balanced political position needs to be reached which simultaneously recognises the priority of enlargement…[and]..maintains structural support, as a matter of continuity, for the enormous convergence effort which the least developed regions in the current Member States have been making and which is nowhere near completion.

- It would be totally intolerable for Portugal if, as a result, of the "statistical convergence" effect, enlargement were to appear to be associated with a toning down of the Union's commitment to the process of correcting the current regional development imbalances.

- It is clear that the volume of financing required to meet this solidarity effort of the structural measures cannot be limited to 0.45 percent of the European Union's GDP".

This intervention was followed up by a letter in January 2002 from the Secretary of State for European Affairs, Teresa Moura, to Commissioner Barnier, in these terms[23]:

- "Maintaining a 0.45 percent GDP allocation for structural policy would reflect a lowered ambition, which could undermine the reinforcement process of social and economic cohesion currently underway.

- Enlargement will lead to a decrease in the average community GDP per capita. We cannot consider that certain regions suddenly become prosperous due to an enrichment which is merely virtual.

- The solution which seems better suited with a view to maintaining the social and economic cohesion principle points to an increase in the reference threshold. The

[22] Address by Elisa Ferreira, Minister of Planning, to the Second European Cohesion Forum, Brussels, 21-22 May 2001.

[23] Letter to Commissioner Barnier from Terses Moura, Secretary of State for European Affairs, Ministério dos Negócios Estrangeiros, Lisbon, 24 January 2002 (unofficial translation)

'phasing out' solution should be applicable only to regions that have already reached real, as opposed to virtual, convergence.

- Social and economic cohesion goes beyond the mere intervention of structural funds….it remains essential to pursue a real and coherent cohesion policy, namely in the areas of agriculture, transeuropean networks, investigation and State aids.

- An appropriate and sustained answer must be given to the asymmetric consequences of enlargement as it does not make any sense that the least developed States should foot a disproportionate part of the bill for the commitments entailed by new memberships."

In ***Italy,*** the headline position of the Italian government on the reform of the Structural Funds was initially characterised in terms of 'Italy threatens to block enlargement'. In May 2001 (in the wake of the 'Aznar Memorandum'), the Treasury and Budget Minister, Giulio Tremonti, was quoted[24] as saying that Italy's support for enlargement was linked to the EU continuing to provide funds for the South: "If there are no compensations for the *Mezzogiorno*, then Italy will ask that the enlargement eastwards be slowed down". More recently, the Italian Finance Minister argued that the share of the allocation of Funds intended for regions lagging behind in development "should be increased by give percentage points" taking account of the importance of thse regions in an enlarged Union.[25]

At official level, the detailed debate on a post-enlargement European regional policy has involved not just inter-ministerial discussions (led by the Ministry of Economy and Finances and the Ministry of Foreign Affairs) but extensive consultations over the past three years with national and regional organisations and around 70 institutional actors. This exercise delivered two documents:

- a memorandum produced in June 2001 on Economic and Social Cohesion, and

- a draft document, a basis for a future memorandum and still to be finalised, prepared in the spring 2002 and currently being examined by regional and national organisations and socio-economic actors.

The main proposals of the first memorandum are threefold (see box):[26] to ensure the impact of EU cohesion policy on the competitiveness of lagging behind regions; to address the needs of candidate countries, whilst guaranteeing highly concentrated interventions in the lagging behind regions of present Member States; and to ensure greater quality, simplification and subsidiarity of EU cohesion policy.

Subsequent debate on the more detailed issues of Structural Fund reform in Italy has highlighted a number of positions. Italy supports a qualitative reinforcement of

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[24] *After Spain, Italy threatens to block enlargement*, EU Observer, 18 May 2001.

[25] CEC (2002) Summary of Discussions in Workshop 1, EC Seminar 'The EU's Regional Priorities – Defining Community Value Added, 27-28 May 2002.

[26] Ministry of Economy and Finances and Ministry of Foreign Affairs, (2001) *Italian Memorandum on Economic and Social Cohesion*, Rome, June 2001.

European regional policy across the whole territory of an enlarged EU rather than any move towards a concentration on the new Member States and a renationalisation in the richer EU-15 countries. Italy favours a retention of the regional focus on EU structural policy, considering this to be more in line with the Treaty, and with support correspondingly focused on Objective 1 regions. The 75 percent threshold should be maintained, although with the option to include wider non-GDP related designation criteria, and some form of compensatory mechanism should be identified for current Objective 1 regions which become ineligible as a result of the statistical effect. Support outside Objective 1 regions could be concentrated on cross-border, trans-national and European-wide initiatives. Lastly, Italy supports keeping the four percent ceiling for Structural Fund receipts in the new Member States because of the potential problems of absorption.

Objectives of post-2006 EU regional policy: the Italian Memorandum

1. *To ensure the impact of EU cohesion policy on the competitiveness of lagging behind regions* - cohesion policy should aim at increasing the competitiveness of regions in candidate countries, as well as in present Member States, by promoting the use of their endogenous resources. In a similar vein as in the Italian Objective 1 CSF, cohesion policy should aim at increasing the regions' productivity (in both lagging behind and more advanced regions) <u>by improving framework conditions rather than by use of aids to enterprises</u> which would enhance rent-shifting conflicts among regions.

2. *To address the needs of candidate countries, whilst guaranteeing highly concentrated interventions in the lagging behind regions of present Member States* - cohesion policy should be more focussed on framework conditions as a means towards the acceleration of economic and social convergence of candidate countries and towards the further contribution to the development of the lagging behind regions in the EU15. An adequate support towards lagging behind regions of present Member States, together with an adequate resource concentration, should be guaranteed by the use of alternative accountable indicators measuring under-utilisation of resources (such as the employment rate) or spatial handicaps, while avoiding fragmentation of resources; and/or a suitable statistical method to measure the prevailing European standard per capita income; and/or the provision of adequate phasing-out mechanisms.

3. *To ensure greater quality, simplification and subsidiarity of EU cohesion policy* - this point relates to the role of cohesion policy at a European level where 'the *quality* of interventions can be enhanced by a high degree of integration among policies implemented in different regions; the *credibility* of policies can be increased if compliance with agreed rules is guaranteed by a common authority; the *consensus* on cohesion policy, which implies resource redistribution, can be strongly reinforced through the co-ordination process allowed by a common policy'. The effectiveness of policy should also be targeted by simplifying procedures, making wider use of evaluation procedures selected according to the principle of subsidiarity; stronger concentration of funds; more clear-cut division of roles between the Commission and the national managing authorities, improved vertical institutional partnership among levels of governance and improved horizontal networking among national and regional authorities in order to increase the exchange of experiences and methods.

3.3 MS perspectives: Continuation of EU regional policy outside lagging regions

Apart from those Member States with large Objective 1 receipts, other countries have also expressed reservations about the prospect of 'renationalisation' of EU regional policy, as expressed in the Dutch paper. While these countries may support a limit on the budget allocated to EU regional policy they are also in favour of continued Structural Funds intervention in tackling problems outside of Objective 1, for example areas undergoing economic and social conversion or with serious geographical or natural handicaps. They generally prefer to retain the current 'regional approach' to implementing the Funds. An illustration of these viewpoints is as follows.

In ***Belgium,*** although there is no official view at federal level, regional ministers (as exemplified by the contribution of Jean-Claude Van Cauwenberghe, the Minister-President of the Walloon Region) have noted that enlargement should not call into question the existence of a regional policy towards those regions in need within the EU-15 and that the Structural Funds should be able to intervene wherever there are persistent regional deficits in economic competitiveness.

The policy debate in ***Finland*** has also advocated continuation of development policies financed by the EU outside Objective 1, albeit with more flexibility in approach. However, an important concern for Finland is the importance of structural problems and depopulation in peripheral parts of the EU, and the need for the special treatment of sparsely populated areas as part of Objective 1 to continue. "Less development areas in Finland (North-Finland and East Finland) should be classified among the highest objective for regional Funds also after 2006".[27]

In ***France,*** the former Prime Minister Lionel Jospin – in a keynote speech on "The future of an enlarged Europe" in May 2001 - strongly argued against the re-nationalisation of "policies that have been so far conducted at the Union level, particularly the Structural Funds". He explained: "it would be paradoxical to suggest steps forward toward a stronger European integration while at the same time starting to operate withdrawals to the national level".[28]

Finally, ***Ireland*** has been cautious about engaging in the debate in view of internal difficulties with ratification of the Nice Treaty and the need for sensitivity on the question of losing Structural Fund receipts. From having been a substantial recipient, Ireland is likely to become a net contributor in future years. As such, the strategic implications for Ireland are to ensure "fair burden sharing" in financing the EU budget and "to keep overall expenditure contained to a level that will minimise as far as possible our net contribution"[29]. However, this is complemented by a desire to

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[27] Speech by the Prime Minister of Finland, Paaro Lipponen, Lieksa, 8 April 2002.

[28] Speech by Lionel Jospin, former Prime Minister of France, 'L'avenir de l'Europe élargie'.

[29] *Ireland and the European Union: Identifying Priorities and Pursuing Goals,* Department of the Taoiseach, Dublin.

ensure a strong role for EU regional policy outside of Objective 1, as indicated by the Irish Minister of Finance, Charlie McCreevy in May 2001[30]:

- "We are strong advocates of a credible cohesion policy after enlargement. By credible, I mean a properly focussed and resourced policy which will ensure that lagging behind regions of the enlarged Union, especially the poorest regions, can be assisted to tackle the economic and social disparities which they face.

- These disparities are especially pronounced in many of the applicant states. Regard will also have to be had to the continuing needs of the poorer regions in the existing Member States and to appropriate transitional arrangement for other regions in these States. I also believe that future Cohesion policy must be able to support national efforts to tackle urban and rural deprivation and social exclusion."

4. CANDIDATE COUNTRY PERSPECTIVES

4.1 Lack of a common position

The ability of the Candidate Countries to find common positions on the reform of EU structural and cohesion policy is limited and the CCs have accordingly placed different emphases on particular aspects of the negotiations. Accession candidates have found difficulty in identifying a coordinated response to the Commission's proposals for several reasons.

First, the EU has never been prepared to carry out accession negotiations with any group of countries. In all cases where enlargement has involved more than one country, the EU has elected to carry out negotiations with each country individually.

Second, the EU has always used its dominant bargaining power to improve further its position in the emerging treaty. This is often achieved by identifying the 'point of least resistance' among several candidate countries, finding a compromise based on this and then using these terms in subsequent negotiations with the rest of the candidates. Slovenia, for example, was the first country provisionally to close the environmental chapter and all the other CCs have subsequently had to accept the 'Slovenia terms' in closing this chapter.

Third, related to the above is the emergence of rivalry amongst CCs in their negotiations with the EU. Delays in Poland's accession negotiations with the EU were criticized by Hungary and Slovakia who said they were not prepared to wait for Poland to catch up before joining the EU.

Lastly, an important barrier to agreement on common positions is the different weighting or mix of interests concerning the chapters. These disparities are due to the different values given to each question on the national priority lists, the diverging levels of preparation in each field, the varied influences of domestic pressure groups,

[30] *Cohesion policy from the point of view of enlargement,* Address by the Minister for Finance, Mr Charlie McCreevy, TD to the Second European Cohesion Forum, Brussels, 22 May 2001.

and the range of public reactions to be expected when negotiating delicate issues. In terms of structural and cohesion policy, the wide variety of institutional frameworks, policy approaches, priorities and domestic pressures make finding a common platform very difficult. For instance, Poland, covering a large geographical area and with a tradition of regional administration, has found it possible to adapt to the EU's model of territorial organization based on the NUTS classification system relatively straightforward. On the other hand, the issues facing small CCs such as Slovenia and the Baltic States are very different. Slovenia, for example, has argued that it represents a special case and has proposed a regionalisation plan dividing the country into three regions which would allow it to use EU regional policy aid to support its poorer regions. The Commission, however, insists that Slovenia should be treated as a single region, a decision which would deprive the country of some regional aid because of the relative prosperity of the Ljubljana region.[31]

4.2 CC responses to future EU structural and cohesion policy

The proposals of the European Commission with regard to the reform of EU structural and cohesion policy have not, to date, provoked major debate in the CCs. At least in the short term, the Commission's proposals seem to be judged as balanced and fair, and negotiators from the CCs are aware that, regardless of the precise details, they are certain to benefit. However, in the long-term, there are some areas of concern for CC-12, stemming from uncertainty over the budgetary framework for future Structural and Cohesion Funds to be allocated by the EU and the direction of EU regional policy after enlargement. All the countries that have accepted the provisions of the chapter on regional policy have reserved the right to return to it once the EU provides more definitive proposals on budgetary allocations.[32] The following points summarise some of the main concerns in the CCs.

4.2.1 Fair and equal treatment

There is a concern that maintaining a four percent of GDP ceiling for regional aid will disadvantage Candidate Countries with lower levels of GDP in comparison to Member States and there is a general expectation that the EU will raise this ceiling. Following a February 2002 meeting in Budapest, the Prime Ministers of four Visegrád countries - the Czech Republic, Hungary, Poland, and Slovakia - urged that "*in the fields of structural and cohesion policy, the candidate countries should receive the same per capita support which is granted to the countries or regions of the EU that are at a similar level of economic development*".[33] Hungary, for example, is unhappy with the level of the proposed rate for the first three years. The EU proposal

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[31] See *EU Accession – Negotiating Positions,* Slovenian Government Public Relations Office, May 2002 and 'Regional and agricultural policy on the agenda as Director General Landaburu visits Slovenia' *Enlargement Weekly 16 July 2002*.

[32] See, for instance, statement by H.E. Antanas Valionis, Head of Negotiations delegation, ministry of Foreign Affairs of the Republic of Lithuania, at the 6th Meeting of Accession Conference with Lithuania, Ministerial Level on 11 June 2002, European Committee under the Government of the Republic of Lithuania.

[33] *Statement of the Prime Ministers of the Visegrad* countries published by the Presidency in Office Budapest, 15 February 2002.

offers just 139 euro/head, which already includes also the cohesion support, while, according to Hungarian calculations, the sum should be at least 219 euro/head.[34]

4.2.2 Low absorption rates

Candidate Countries recognize that, in terms of administrative capacity, absorbing Structural Funds is not easy, especially in the first two years of a programming period. Experience from the EU-15 shows that even current Member States can absorb very low amounts of funds in the first year of multi-annual programmes. Some of the new Member States are not sure that they will have the administrative capacity to start their three-year programmes (2004-2006) by accession. Some estimates for Poland, for example, envisage absorption rates as low as ca. 20 percent of available funds.[35]

The level of co-funding and the availability of Government budgetary resources will also be critical limiting factors on absorption. Many of the CCs are attempting to exercise budgetary restraint while social needs and the burden of meeting the terms of the Accession Treaty in areas like the environment apply additional pressures. For areas qualifying for Objective 1 status, which is likely to be most of the Central and Eastern European CCs, the European Commission is prepared to contribute up to 75 percent of all public investment costs – requiring the remaining 25 percent to be found from other sources. This could be a significant challenge for many of the CCs. In the case of Estonia, for example, depending on the rate of economic growth, Structural Fund support equalling four percent of GDP could potentially result in annual Structural Funds support of €400 million. This would require the Estonian public authorities to identify co-financing of ca. €133 million, a figure which is higher than the current budget for all public investments, including many areas of expenditure ineligible for Structural Fund support. However, there is also concern in other CC-12 countries that absorption capacities have been underestimated and that the continual improvement in this situation has been disregarded. These countries fear that extending the four percent of GDP threshold beyond 2006 will begin to handicap countries which can use the funds wisely.

4.2.3 Regional polarization after enlargement

There is also concern amongst CC-12 countries regarding the EU's approach to structural and cohesion policy after enlargement. Candidate countries fear that, without increasing the budget for financing future cohesion policy, reform solutions could result in CC-12 regions receiving less assistance than the Objective 1 regions of

[34] According to these calculations, Hungary would receive €1 billion from the Structural and Cohesion Funds in 2004, and €1.2 and €1.4 billion in 2005 and 2006 respectively, whereas Portugal, one of the poorer Member States - with exactly the same area and population as Hungary but with approximately double Hungary's GDP per capita rate - received €3.6 billion euro in regional aid in 1999.

[35] 'BCC Expert: Poland will Be Able to Use Only 17 Percent of EU Funds' *Warsaw, July 15 Polish Daily News Bulletin 16 July 2002.*

the present Union after the enlargement - a result considered politically unacceptable.[36]

Some reform options could launch a radical departure from previous practice. For instance, shifting more responsibility for regional development back to the national level (the proposed 'renationalisation' process) would penalise countries in the CCs with limited domestic resources. Similarly, the debated move from traditional infrastructure development assistance to a focus on human capital and the information society would disadvantage regions in the CCs where basic infrastructure investments are still badly needed. Increasing disparities have been noted between growth centers in some CC regions (usually associated with capital city-based agglomerations) and poorer, economically developed regions (usually located in peripheral, rural areas). For instance, the Slovenian negotiating position on Chapter 21 draws attention to "great disparities in terms of distribution of jobs, the unemployment rate, the educational structure of the population, inadequate transport links between regions and uneven access to social infrastructure within regions. The problems are particularly pressing in the structurally less-developed, economically weaker and predominantly agrarian regions".[37] A fear persists that post-enlargement reforms could favour 'richer poor regions' over 'poorer poor regions'. Slovenian Prime Minister Drnovesk recently warned against enlargement creating "new divisions between big and small, haves and have-nots".[38]

5. REFORM ISSUES: BUDGETARY PARAMETERS

Turning from the political debate to the substantive issues associated with reform, the October 2001 report to Sponsors reviewed a range of academic and policy research relating to scenarios and estimates of the implications of enlargement for EU regional policy (as shown in the box below)[39]. As noted in the report, the studies each have

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[36] Speech by the Prime Minister of Poland, Mr. Jerzy Bużek at the 'Forum on Economic and Social Cohesion' (Brussels, 22 May 2001).

[37] *Republic of Slovenia Negotiating Position on Chapter 21* Ljubljana, 30 November 1999, www.gov.si/ops/datoteke/pi/ang/21.doc

[38] Country Profile: Slovenia BBCi News 9 August 2002.

[39] IBO (2001) *The financing of the EU structural policy in the context of the enlargement of the EU*, Interdepartmental Policy Study, The Hague. DIW (2001) *Reformbedarf bei den EU-Politiken im Zuge der Osterweiterung der EU*, Report to the Federal Ministry of Finance, Deutsches Institut für Wirtschaftsforschung, Institut für Agrarökonomie (Georg-August-Universität) and Institut für Europäische Politik, Berlin and Göttingen. Dresdner Bank (2001) *The Challenge of Enlargement, Economic Analyses* – Trends Special, July 2001, Dresdner Bank, Frankfurt/Main. European Parliament (2001) *Working document on the financial implications of EU enlargement*, Committee on Budgets, European Parliament, 11 April 2001. Schrumpf H and Budde R (2001) *Die Auswirkungen der Osterweiterung auf die Regionalpolitik der Europäischen Union*, Schriften und Materialien zur Regionalforschung, 8, Rheinisch-Westfälisches Institut für Wirtschaftsforschung, Essen. Bachtler J, Wishlade F and Yuill D (2000) *Regional Policy in Europe after Enlargement*, European Policy Research Paper, No. 44, EPRC, University of Strathclyde, Glasgow.

different methodologies and assumptions, applied to different policy scenarios, and the outcomes are not directly comparable. Nevertheless, they revealed the possible spread of enlargement costs over the 2007-2013 period, ranging from €115 billion to almost €240 billion. Leaving aside the top figure in the range (from the Dresdner Bank study, which was predicated on an assumption that the Objective 1 threshold will be raised to retain the eligibility of the current Objective 1 regions), the average of the estimates suggested that the costs of enlargement could be around €150 billion over the 2007-2013, or an average of €21 billion per year.

Studies on the scenarios and costs of enlargement

- DIW study – comprehensive and detailed analysis by the Deutsches Institut für Wirtschaftsforschung (German Institute for Economic Research) for the German Federal Ministry of Finance (May 2001), presenting scenarios for enlargement and calculating the costs
- Dresdner Bank study – comprehensive review of the 'challenges of enlargement' (April 2001), identifying economic and budgetary consequences for applicant and EU countries
- EPRC study – for the 'Sub Rosa' Seminar 'Regional Policy in Europe After Enlargement' (September 2000), examining the enlargement implications for EU regional policy, EU competition policy and national regional policies and presenting four options for Structural Fund reform
- European Parliament study – review of EC, CC and research institute perspectives on enlargement and presentation of budgetary costs according to different parameters
- IBO study – interdepartmental study (2001) carried out for the Dutch government to review scenarios for reforming EU structural policy and the implications for the Netherlands
- RWI study – by the Rhine-Westphalia Institute for Economic Research, calculating the budgetary implications of the changes to area designation criteria in an enlarged EU, as proposed by the EC in the Second Cohesion Report

Over the past year, several new studies have been produced with further insights into the budgetary implications of enlargement. The following sections provide a brief outline of the methodological approach and results of the studies.

5.1 Osteuropa-Institute (Quaissar and Hall)

This Quaissar and Hall study[40] examines the economics of enlargement including growth and welfare effects and the impact of trade, FDI and migration on labour markets. It also provides an overview of the institutional and policy reforms required by enlargement, including a debate on future structural and regional policy and the reform of the CAP.

Methodological Assumptions

EU budget scenarios

Accession assumption:

- Option 1 'Group entry': Poland, Hungary, the Czech Republic, Slovenia, Estonia, Cyprus and Malta entering in 2004, Slovakia, Latvia and Lithuania in 2006 and Bulgaria and Romania around 2008
- Option 2 'Big Bang': accession of CC-8 and IE-2 in late 2004 or 2005 with Romania and Bulgaria following in 2008 (considered to be favoured by European Commission)

Growth assumptions:

- 2.5% in EU-15 and 4.0% in CC-10

Structural Fund assumptions:

- accession of Romania and Bulgaria in 2008 with Structural Fund transfers of 4% of GDP

Other assumptions:

- Structural Funds decrease at annual rate 1.23%, agricultural funds increase by 0.63%
- Structural Funds will reach 4% limit and agricultural transfers include direct payments – initial phasing in but maximum levels by 2007

In overall budgetary terms, the study notes that various researchers (regardless of methodology) have estimated the financial costs of the first accession round of five candidate countries to be between 0.1 and 0.2 percent of the current EU-15 GNP. While the accession of a larger number of countries would increase the financial burden of enlargement, the weight of this burden is expected to decline as the accession date becomes later. It is estimated that nine billion euro less than EU estimates would be spent between 2000-06 because of the later accession date. The cost calculations do not alter significantly with a Big Bang scenario; on the basis of enlargement costs only "*the Big Bang scenario is by far the most advantageous for the EU*". The real cost burdens will start to emerge after 2007.

Based on the EU budget scenarios, total transfers are expected to rise from €8.2 to €21.3 billion in 2008 (including Romania and Bulgaria). Total enlargement costs are estimated at €20.5 billion for EU-25 in 2006 in the case of a 'Big Bang' accession or €22.4 billion for a Group entry. These costs would rise in an EU-27 in 2008 to €34 billion, corresponding to 0.35 percent of EU GNP. Assuming that net welfare gains to the EU-15 are 0.5 percent of EU-15 GNP (estimated in a number of models), this

[40] Quaissar W and Hall J (2002) *Toward Agenda 2007: Preparing the EU for Eastern Enlargement*, Working Paper No. 240, Osteuropa-Institut München.

would offset the enlargement costs. Structural policy expenditure is understood to be the most dynamic cost factor in the medium- to long-term, partly because of the link to GDP growth.

The study points out the imbalances in the degree of financial redistribution related to per capita GDP (eg. why does Ireland receive, in net terms, much more per capita related to its national wealth than Spain?). A fundamental reform of the EU financial system is proposed whereby funds should be distributed according to countries' national GDP per capita, measured in PPS. The maximum amount of funds would be fixed in advance, either as a lump sum or a specified percentage of the EU budget or total EU GDP. This could be applied either just to structural policy or to both agricultural and structural expenditure. To support enlargement, the funds would be concentrated on the lowest income countries of the new Member States.

A proposal for the Structural Funds is to set the financial limit at 0.35 percent of EU GDP, with €37 billion allocated for the whole 2007-13 financial period. Payments would be distributed reciprocally based on the per capita GDP ranking among Member States in each financial year together with a 'distribution factor' representing the differences between the EU per capita GDP average and the per capita GDP of individual Member States. The background to this recommendation is the view of the study that CAP and structural policy in their current forms should be abolished and policy intervention limited to the regulatory supervision of national programmes. The budgetary savings would offer additional room for national government spending in these areas based on their own priorities, freeing EU budgets for expenditure in other areas (eg. security, internal market, education etc.).

5.2 CEPR (Vaitilingam, Boeri et al)

The CEPR study[41] covers several aspects of enlargement causing particular popular concern: labour markets; social welfare; East-West migration; and regional policy. The regional policy analysis looks at the effectiveness of structural policies in accelerating income convergence (including the likely positive impact of investment in educational infrastructure), before examining how to share the costs of redistributive policies and allocate the funds. The report comments that, in the light of the evidence that the Structural Funds have contributed to growth in some countries, the cost of enlargement should not fall primarily on the current beneficiaries of the Funds given that curtailment could mean significant cost in terms of convergence in the EU-15.

[41] Vaitilingam R (Ed), Boeri T et al (2002) Who's Afraid of the Big Enlargement? Economic and Social Implications of the European Union's Prospective Eastern Expansion *CEPR Policy Paper No. 7,* Centre for Economic Policy Research, London, June 2002).

Methodological Assumptions

Accession assumption:

- enlargement to CC-8 and Cyprus in first phase

Other assumptions:

- phasing-in of Structural Funds to allow for absorption by new Member States
- income differences between new and current Member States will diminish over time, reducing the need for transfers.

The study estimates the future EU budgetary costs based on a continuation of the current redistribution co-efficient of 5.76 percent for the 1998 budget. This co-efficient, calculated by de la Fuenta and Doménech[42], assumes that for a typical European citizen, the net effect of the EU budget is equivalent to a flat tax of 5.76 percent on the difference between individual gross income (adjusted for purchasing power differences) and the EU average, or to a subsidy of the same magnitude if individual income is below average.

Net budget surpluses per head in PPS are obtained by multiplying the difference between each country's real income per head and the average value of the same variable in an enlarged EU composed of current members, CC-8 and Cyprus. If the current degree of redistribution through the EU budget is maintained, most of the new members would receive significant net transfers, ranging from 0.69 percent of GDP (Cyprus) to 13.25 percent (Latvia). The sum of the required transfers is €19.5 billion, or 0.25 percent of EU-15 GDP which could be accommodated by the EU budget without violating the 1.27 percent of GNP resource ceiling. The expenditure earmarked for enlargement at Berlin was €14.2 billion in 2006, leaving a margin of €12.8 billion for potential expenditure within the 1.27 percent ceiling – the sum of these figures is sufficient to fund the full integration of the CC-8 and Cyprus in 2006.

In terms of the distribution of the future EU budgetary costs, the de la Fuenta and Doménech study highlights the excess balances of the EU-15 in 1998, based on the net contribution of each Member State to the EU budget over and above what would be required for its income per head and estimated redistribution coefficient. This calculation shows Germany contributing €3.5 billion more than it should while France falls short by €4.1 billion (more than Greece, with a figure of €1.3 billion below). The study recommends revising the current budget practices to ensure greater horizontal equity while maintaining the current degree of redistribution and extending it to new members.

5.3 Stiftung Wissenschaft und Politik (Axt)

This study by Heinz-Jürgen Axt[43] looks specifically at EU structural policy and the need for reform in the light of enlargement, drawing partly on the findings of other research. It presents an overview of the range of options for reform and summarises

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[42] De la Fuente, A and Doménech, R (2001) The Redistributive Effects of the EU Budget: An Analysis and a Proposal for Reform, *Journal of Common Market Studies*, Vol. 39:2

[43] Axt H-J (2002) *Die Strukturpolitik und die EU-Erweiterung – Substantielle Reformen unabdingbar, aber politisch schwer durchzusetzen* SWP-Studie, Stiftung Wissenschaft und Politik.

the main discussion, with a specific look at the implications of structural and cohesion policy reform for Germany.

The study concludes that, without substantial reform of EU structural policy, the available financial resources will not be sufficient to cover enlargement-related costs - even with growth rates of 2.5 percent for the EU-15 and 4.6 percent for the CC-12. An important factor will be the extent to which the 75 percent threshold for Objective 1 designation (assuming a continuation of the current policy approach) is applied strictly. The more modifications which are made to allow continued eligibility of current Objective 1 regions, the greater the financial shortfall likely to be encountered in the EU budget. The lower budgetary estimates in some studies (eg. Weise *et al* – see above) are contingent on these reductions in current Member States taking place but often take insufficient account of the political likelihood of their approval.

In terms of the financial implications of reform, the report looks at the different outcomes of a regional or national-led approach to policy change. Under a region-led reform, the resources required for the Structural Funds under Agenda 2000 would halve from €239.4 billion for 2000-06 to €111 billion. The saved money could be made available for national level action to combat regional disparities within Member States, enlarge the financial allocation for the candidate countries and provide phasing out support for de-designated regions. Overall, it would mean that there were sufficient resources to fund enlargement and aid would be targeted on the neediest regions in the EU-15. Of the current Cohesion countries, only Spain would be impacted by the withdrawal of Objectives 2 and 3.

Under a country-led reform model, the threshold level for eligibility would have important impacts on the required budget. The retention of a 75 percent threshold in an EU-20 would reduce funding for Objective 1 areas in the EU-15 from €17.2 billion to €10.4 billion and, in an EU-27, the reduction would be to only €5 billion. A 86.7 percent threshold in an EU-27 would raise the amount available in the EU-15 to €9 billion. In overall terms, an additional €27.3 billion would be required for Structural Fund expenditure in new Member States in an EU-27 with the retention of a 75 percent threshold and an additional €27.8 billion with a 86.7 percent threshold. These expenditure levels could only be financed if the 1.27 percent own resources limit of the EU was fully used and the extension of agricultural policy was cost-neutral.

5.4 CPB (Ederveen et al)

The CPB study[44] looks primarily at the structure and effectiveness of current cohesion policy, weighing evidence of its impact on convergence levels. The final section looks forward to the future of cohesion policy, drawing its figures mainly from the IBO study (see above). It highlights a range of dilemmas which face the reform of cohesion policy before outlining three main reform options.

The first option (‘control’) keeps the institutional structure virtually unchanged with a greater involvement of the EC through increased monitoring, evaluation and tighter rules and regulations. The downside of this option would be the potential to increase

[44] Ederveen S, Gorter J, de Mooij R and Nahuis R (2002) *Funds and Games – the Economics of European Cohesion Policy* CPB Netherlands Bureau for Economic Policy Analysis, The Hague.

administrative costs for national and regional governments without necessarily increasing policy effectiveness.

Under the second option ('competition'), the European Council sets the total budget for cohesion support for the programming period and national or regional governments apply for funding on the basis of project proposals. The EC is responsible for project assessment using a series of objective criteria (eg. welfare level of region/country; expected investment return; cross-border spillover effect). Co-financing would be dependent on the welfare level of the country which would improve the distributional efficiency of cohesion support and increase the absorption capacity in new Member States. Problems with this option include the potential for political or pressure group lobbying and the possibility that high administrative requirements could be imposed on governments applying for funds.

The third option ('flexibility') reforms cohesion policy into a system of fiscal transfers at country level. The European Council decides each planning period about the allocation of funds based on political priorities. This option is consistent with subsidiarity and the lack of absorption capacity in poor Member States would no longer be a problem. Difficulties with this approach include its vulnerability to government failures, particularly in countries lacking an effective and transparent public administration. Financial support would, therefore, be linked to conditions regarding institutional reform and sound economic policies.

5.5 Costs of enlargement

The main budgetary conclusions of the October 2001 report to Sponsors was that enlargement could imply an additional cost for EU structural and cohesion policies of ca. €21 billion per year. Estimates at the lower end of the spectrum projected costs of around €12 billion per year with higher assessments ranging to almost €30 billion per year. Taking account of the fact that the EU is already budgeting for an annual cost of post-enlargement structural operations of €12 billion, the 'gap' between what is required and what is available may be as high as €18 billion but, more likely, will be in the range €9-10 billion.

The budgetary projections of the most recent studies broadly substantiate these figures. Indeed, in two cases, the estimates are very similar to the previous €21 billion figure. Based on EU budget scenarios, Quaissar and Hall forecast total EU transfer costs of €21.3 billion euro in 2008 (including Romania and Bulgaria) while the CEPR study estimates transfers of €19.5 billion based on a continuation of the current redistribution co-efficient. The Axt study, which draws on the high estimates of the Dresdner Bank study, is the main exception and states categorically that, without substantial reform of EU structural policy, the available financial resources will be insufficient to cover enlargement-related costs.

The studies highlight a range of factors influencing the final budgetary calculations. These relate generally to the particular methodological focus of the research and are not always directly comparable but some issues are worth mentioning. The first is the impact of the timing of EU enlargement. Quaissar and Hall point to the mitigating budgetary impact of a later accession date, which would offset the greater financial burden of a higher number of countries joining the EU. They conclude that the 'Big Bang' scenario of the simultaneous accession of ten candidate countries (ie. excluding

Romania and Bulgaria) would be the most advantageous for the EU in terms of enlargement costs and that the real cost burdens for the EU will begin to emerge from 2007.

A second critical factor for future budgetary projections is the nature of any reform of EU structural and cohesion policies. Of particular importance is the extent to which Objective 1 regions in the current EU-15 will retain eligibility in an enlarged EU. Given the economic development levels of most of the Candidate Countries, the application of a 75 percent or a higher 86.7 percent threshold for Objective 1 eligibility would make little difference to the additional finance required for new Member States in an EU-27. Axt calculates that an additional €27.3 billion would be required for new Member States with a 75 percent threshold and an additional €27.8 billion with an 86.7 percent threshold. The threshold setting will have a much greater budgetary impact on the current EU-15 - a 75 percent threshold in an EU-27 would see a reduction in funding for current Member States to only €5 million euro, rising to €9 billion with an 86.7 percent threshold. Essentially, Axt points to the fact that the lower budgetary estimates of some earlier studies are contingent on sharp reductions taking place in Objective 1 coverage in current Member States – a development which may prove to be politically difficult.

6. REFORM ISSUES: IMPLEMENTATION OF THE FUNDS

6.1 Allocation options

It is evident from the previous discussion of Member State and Candidate Country perspectives on the reform debate that there are significant differences in view as to how EU regional policy should be allocated in future. As yet, the debate has been conducted at a relatively general level with contributors mostly discussing the principles of allocation rather than specific methods or criteria.

On one side of the argument are the proponents of retaining a well-funded EU regional policy intervening in a wide range of areas and activities. As previously noted,[45] the implication of the above studies is that there is potentially more flexibility in the allocation of Structural Funds than was originally assumed. This would allow a variant of the '***status quo option'*** to be maintained.

Under this option, the Structural and Cohesion Funds are extended eastwards but the absorption limit puts a cap on the amounts transferred to the Candidate Countries, permitting the EU to continue providing significant support for the lagging regions in the EU-15 and also intervening in support of other horizontal and thematic development priorities. The advantage of this approach is that it contributes to the political cohesion of the EU since most or all Member States would receive some Structural Funds, and – importantly – it ensures that the 'net payers' retain a vested interest in EU regional policy. The main disadvantage is the prospect of non-Objective 1 funding being spread very thinly across numerous small areas with a

[45] Bachtler J (2001) *op. cit.*

disproportionate administrative bureaucracy to deliver the Structural Funds in these areas.

This option appears to be the preference of the Commission at present, at least within DG REGIO. It would retain Objective 1 as the priority for EU regional policy, applying the current threshold of 75 percent of EU GDP per capita, although the treatment of Objective 1 regions rendered 'ineligible' by virtue of the statistical effect is still an open question. EU regional policy would still have a role outside Objective 1 with a successor to Objective 2 encompassing a range of development priorities, as noted earlier (see Section 2.1). Co-operation between regions through inter-regional, transnational, cross-border and networking activities would also be retained.

The current main alternative to this is the ***'cohesion policy option'*** put forward in the Dutch non-paper. This would allocate EU regional policy resources according to a national eligibility criterion to focus on the poorest Member States, effectively withdrawing Structural Funds from the disadvantaged areas of richer countries. Other support could be provided for activities, such as transnational co-operation, in both richer and poorer countries where such activities have 'truly added Community value'.

The advantage of this approach is that structural policy would become a Community policy with an economic rationale for intervention, focusing on convergence among Member States. It would avoid the so-called circular flow of income from net payers to the Commission and back again and would overcome problems of inadequate designation indicators and data. The approach would allow recipient countries to take a national approach to the design and delivery of policy to suit national conditions, and the implementation of policy would become more manageable for the Commission.

The potential 'downside' is that net payers would not be recipients of EU funding, possibly lessening their financial commitment to the EU and to structural policy in particular. The Commission would not have a 'place at the table' in all countries, and the profile of the EU could thereby be potentially diminished. Pressure for spending in areas where the current richer members could benefit more may be increased (aspects of agricultural policy, R&D policy) as may pressure for relaxation of the regulatory environment, especially in the area of national regional aid. Lastly, with a focus on Member State level convergence, and depending on the development priorities set by individual recipient countries, there is the potential for increased regional disparities within national boundaries.

6.2 Implementation mechanisms

Apart from the issue of financial allocations, the system for implementing the Funds after 2006 is an important topic in the reform debate. Most Member States are concerned about the administrative complexity and bureaucracy of the Funds which has led to demands for simplification, both before as well as after 2006 (see Section 7 below). There are also concerns with the fundamental 'added value' of the current system and the degree to which the management and administrative procedures improve the quality of economic development interventions. These issues are particularly relevant for those Member States that would receive limited Structural Fund resources after 2006.

In considering the range of future options, at one end of the debate is the proposal for a ***budgetary transfer mechanism***, which is implied by the some of the Dutch and German contributions. Under this option, Member States operate their own regional policies, with the EU financing part of the national policies and programmes by a budgetary transfer from the EU to the Member State. This would have the advantage of being straightforward to apply, especially in the richer Member States where the amounts would be small, and it would give Member State authorities maximum flexibility in selecting the priorities and areas of support. On the other hand, such a system would have very weak Community value; it would be difficult to ensure that expenditure was contributing to Community objectives. These objections could be overcome by some form of contractual agreement between the Commission and each Member State on the specific outputs to be achieved, or some other conditionality in the provision of expenditure, although this might be difficult where small amounts of expenditure were involved.

At the other end of the spectrum, is a ***simplified version of the existing mechanism***. This option would be a variant of the current approach whereby the Commission adopts the list of eligible regions under the spatial objectives and negotiates and approves the content of CSFs, SPDs and OPs and their financing plans as well as influencing or controlling the monitoring, financial management and evaluation of interventions. As indicated in Section 7 below, the Commission has already identified scope for simplification in a range of areas within the current regulatory framework. Under new regulations after 2006, simplification could be extended with the transfer of more implementation responsibilities to the Member State level. Such an approach would enable the Commission to ensure that EU objectives are being addressed within Structural Fund programmes and also that important principles, such as the involvement of partners in development programmes, are being respected. On the other hand, it is likely that even a simplified version of the current approach would not be acceptable to those Member States in receipt of small amounts of Structural Fund support. It is also difficult to see how the fundamental tension between the Commission's responsibility for the execution of the EU budget and the desire for simplification can be resolved since some forms of Commission monitoring, financial control, evaluation and audit would continue to be necessary.

An intermediate approach being considered by DG REGIO is for a differential implementation system, retaining the current mechanism for the large amounts of expenditure under Objective 1 but to adopt a ***menu approach*** for Objective 2 (or its successor). This would involve selecting a limited number of thematic and territorial priorities at EU level, for example:

- thematic priorities: the new economy and information society, sustainable development and networking;
- territorial priorities: urban zones, industrial re-conversion zones, rural areas, areas with permanent natural handicaps, co-operation between regions.

Under this approach, the Member States could be responsible for spatial targeting of support. This would seem to involve the 'indirect zoning' suggested in the Second Cohesion Report whereby eligible areas would be decided by national governments on the basis of a set of parameters established by the Commission (as adopted for some Community Initiatives). The practical implications of implementing the 'menu

approach' are still unclear, although some form of 'tripartite contract' between the region, Member State and the Commission has been suggested by Commission services.

The main advantage of this approach would be flexibility. There could be a direct link between EU regional policy and the wider 'competitiveness agenda' of the EU, and individual Member States would be able to select areas of support which suit their needs and individual policy priorities. Spatial targeting could also potentially be adapted to suit individual needs, although the State aid rules – and the issue of coherence between Structural Fund and national regional aid maps – would be a constraint. A key question is whether the menu approach would deliver a simplified system of implementation; the suggestion of a 'tripartite contract' could merely be a variant of the current approach to managing the delivery of the Structural Funds, which would not meet the requirements of several Member States, as noted above.

7. REFORM ISSUES: SIMPLIFICATION OF MANAGEMENT

7.1 The simplification debate

The issue of simplification is not only a concern for post-2006 EU regional policy. It is also highly relevant for the current programming period and has been one of the dominant issues in relations between the Commission and Member States over the past year. Simplification was one of the main objectives of Agenda 2000 and the Berlin Council agreement. However, in practice the process of implementing the Structural Funds has become more complex. Decentralised management has been accompanied by stricter requirements with respect to financial control, audit, monitoring and evaluation. Based on the experience of the first 2-3 years of the new programming period, Member States have put pressure on the Commission to simplify the implementation process.

At the Namur Informal Council, *"the representatives of the Member States expressed considerable concern about the risk of not achieving the goal of greater simplification linked to decentralisation because of implementation of the rules on financial management and supervision by the Commission"*[46]. Subsequently, the United Kingdom took a lead role in the debate by producing a paper on simplification which was discussed at a meeting of the CDCR in March 2002. The Commission then undertook its own consultations and analysis, which identified the need to address the question of simplification at both political and technical levels. Among the proposals was the need to engage in high-level discussions on simplification within the Commission (which took place in Summer 2002), and with Ministers, leading to the organisation of a Ministerial Meeting on 7 October 2002.

The Commission's agenda for discussion contains a wide range of simplification proposals. At one level, some of the issues of concern are relatively minor and could be addressed speedily by more information, clarification of requirements by the

[46] CEC (2002) *op.cit.*

Commission or a revision of guidance to rationalise administration. Other aspects are more substantive, notably the amount of audit, the application of the performance reserve and the decommitment rule (N+2), where current problems, and potential changes, have major political and administrative implications for the implementation of the Funds.

7.2 Causes of complexity

As a starting point, it is important to be clear about the reasons for the ‘complexity’ of the Structural Funds and why simplification is necessary. In terms of fundamental reasons, the Commission is correct in pointing to the tensions inherent in Treaty provisions that share responsibilities between the EC and Member States, although there is clearly scope for differing interpretations of how ‘responsibility for implementation’ should be defined. It is also the case that the regulatory framework established at Berlin involved a decentralisation of responsibilities to the Member State in return for stricter financial management conditions and more scope for the Commission to audit Member State systems. Clearly, the Commission also has responsibility for accounting to the European Parliament and the Court of Auditors for management of the Funds and for which the Commission has frequently been criticised by these bodies in the past. All of these factors contribute to the increased demands placed on Member States, especially in the areas of financial control and audit.

However, there are several, specific institutional and administrative factors that contribute to the complexity issue.

First, the separation of the funds, with separate institutional responsibilities at EC level (generally replicated at national level) and separate systems of management, evaluation and control is a fundamental cause of complexity. It is the individual programmes or sub-programmes that have to co-ordinate the resources from the different Funds in practice. As the Commission have themselves recognised, the institutional divisions are also reflected in lack of timely and effective liaison and co-ordination between the services of the EC in areas such as monitoring, evaluation, financial control and audit.

Second, programming has not been simplified – rather, the reverse has happened. By comparison with the first generation of Structural Funds (1989-93), the current generation of programmes cover a wider range of: (a) areas of intervention; (b) policy priorities, most recently with the greater emphasis placed on equal opportunities, environmental sustainability, social inclusion and the information society; and (c) types of instrument, especially in the field of financial engineering. During the programme preparation phase, it was common for regions to speak of ‘policy overload’, which is evident in the substantial increase in the volume and complexity of the programming documents – very substantially so in some cases. In the view of several Member States, the split between Single Programming Documents and Programme Complements did not lead to a rationalisation of the information required, particularly because of the lack of clarity about which information needed to be included. These complex policy documents now have to be implemented in practice.

Third, it is not just the financial management requirements that have become stricter but also the requirements for monitoring physical outcomes, results and impacts. In many Member States and regions, these have required considerable investment in new administrative procedures, such as IT-based data collection and analysis systems. They also involve more work at the beneficiary and project level to ensure that the quality of application and monitoring data is increased.

Fourth, some of the changes in complexity are directly attributable to decisions in the Member States. Particularly in those countries/regions which are expecting to lose most or all of their Structural Fund resources after 2006, there has been a widespread effort to maximise the efficiency and effectiveness of the 2000-06 programmes in the interests of leaving a 'durable legacy'. This is evident in the changes made to management systems and administrative procedures, especially with respect to project generation, appraisal and selection, with a view to improving the quality of projects. There is also evidence of more complicated programming structures, for example using intermediary bodies or partnership groups to deliver the Funds 'closer to the ground'.

Fifth, there are specific problems facing Objective 2 areas where the reduction in eligibility has sometimes led to very patchy coverage – for example, separating out eligible 'areas of need' from ineligible 'areas of opportunity' within the same labour market area. This creates specific challenges for the strategic management of the programme as does the different conditions applying to designated and transitional areas. In many Objective 2 areas, there has also been a significant shift away from infrastructure towards supporting more 'intangible' areas of support, such as innovation, technology transfer, information and advice systems. By comparison with the relative 'simplicity' of spending on infrastructure projects, absorption of funding under the more innovative measures is sometimes proving to be a real problem, again requiring more time in working with applicants. Many Objective 2 programmes were also launched late (especially in Italy) which has compressed the timescale for launching the programmes, dealing with a backlog of applications that built up during 2000 and the first half of 2001 and now preparing the mid-term evaluation.

Lastly, in the current 'audit culture', Member States are very aware of the need to ensure that their management of the Funds not only conforms to high professional standards but that implementation is being undertaken in accordance with the Commission's interpretation of the regulations. They have previous experience of the pre-2000 programming periods when the interpretation of national programming authorities could and would be challenged and corrected by the Commission. In the current programming environment, where audit is much more prevalent, and where programming mistakes could lead to penalties via the decommitment rule or performance reserve, it is not surprising that programme authorities are frequently keen to seek guidance and clarification from the Commission. It has to be remembered that, in some Member States (eg. Netherlands, Sweden, UK), the allocation of EU resources is being undertaken through separate, Structural Fund-specific project selection systems which have been especially established for this purpose and are therefore potentially more exposed if something goes wrong.

7.3 Proposals for simplification

The initiative of the European Commission in bringing forward proposals for the simplification of the operation of the Structural Funds represents an important step forward.[47] By contrast with some previous discussions of simplification (eg. the CDCR seminar on 19 March 2002), when the Commission reacted defensively or with ad hoc responses, the present approach recognises both the political and technical aspects of the debate and adopts a constructive, systematic process of clarifying the nature of the problems and putting forward possible solutions. The Commission also makes important commitments to delivering administrative changes by certain deadlines.

The Commission makes an extensive range of useful suggestions, many of which involve action on the part of Commission services. (Specific observations on the individual proposals are provided in Table 1). Actions include providing more guidance and information, undertaking further work to simplify certain procedures, engaging in discussions with Member States and other bodies on specific issues, and changing internal procedures (notably better inter-services consultation). It is less clear, however, to what extent these can be followed through. At a time when the Commission services already have a projected heavy workload (mid-term evaluations, mid-term reviews, allocation of the performance reserve, reform of the Funds etc), it is not necessarily certain that the Commission has the resources and management arrangements to deliver on its proposals.

Finally, the Commission has drawn attention to the need for the simplification debate to lead to permanent improvements and for the lessons learned to be applied to the implementation of the Structural Funds in the Candidate Countries. It will be important for some kind of permanent forum to be established that can monitor the delivery of the simplification measures agreed and ensure that further, on-going rationalisation can be discussed. A further point concerns the role of national governments. During the simplification debate, Member States have been rightly critical of the Commission as causing excessive complexity in Structural Fund management. On the other hand, Member States need to recognise that they themselves agreed the regulatory framework at Berlin, and the Commission is right in arguing that Member States share the responsibility for simplifying the process.

[47] CEC (2002) *Note on the simplification, clarification, coordination and flexibility of Structural Fund management in the period 2000-06*, Commission of the European Communities, Brussels.

Table 1: Simplification proposals

Area of simplification	Issues	Commission Proposals	Comments
Adjusting the programmes	• Need for greater flexibility in modifying programmes. Some adjustments currently possible (to programme document and complement) but MSs would like more scope for practical management-related changes (eg. responding to unexpected variation in take-up rates)	• *De facto* and regulatory context determine scope for possible adjustments • Adjustments have to be approved by Monitoring Committees in advance with subsequent EC decision within 4 months - EC committed to deciding well within this deadline	• Practical experience shows that programme adjustments take longer than stated • Options for further expediting process include shorter target times for EC or ability of Managing Authorities to get preliminary approval from EC prior to final Monitoring Committee decision
Inspections / Controls	• Control requirements on MSs considered too prescriptive and detailed • MS concern of number of audits by Commission and other bodies (eg. OLAF, Court of Auditors) and lack of coordination. • Controls still necessary – evidence of irregularities at all levels (variation between MSs)	• Provision of clearer reference/best practice guides for MS controls • Series of detailed suggestions to improve coordination between SF audit departments, OLAF, Court of Auditors and MS audit activities. Include: improved planning/ transparency ./coordination of activities, and timely feedback; annual statement of assurance for programmes; streamlined reporting • Ultimate aim of 'total audit concept'	• Given number of bodies involved, extent to which increased coordination can genuinely be achieved in short- to medium-term is uncertain • Lack of strong commitment by EC to creation of single audit service for all SFs • More immediate potential in certain specific EC suggestions – although some would require legislative change and effectiveness would influenced by coor-dination with audit activities of other bodies
Mid-term review	• Requirement for comprehensive exercise bringing together various elements with sometimes incompatible timing • Need for rapid operationalisation of any agreed changes	• Simple guidelines, streamlined consultation and decision-making (eg. single EC decisions on revisions; modification decision by EC in 2 months if request well prepared) • No renegotiation of interventions	• Commission proposals positive, particularly on timescale of decision-making • Timing of Monitoring Committee meetings to approve modification proposals could be autumn 2003 - early than EC indications
Reports	• Too many reports required based on overly detailed and sometimes retroactive EC guidelines with unclear added value of some information	• Standardised presentation of information, option for combined annual report, reduction in level of detail	• Positive EC proposals – potential for proportionality to be stressed more and clarification on areas where minimum levels of information could be provided

Result and Impact Indicators	• Quantification problems given range of indicators, programme levels and objectives • Complex data collection and monitoring systems with insufficient distinction between areas of primary/secondary importance	• Shake-up of systems counter-productive • Potential for assessment of options for individual programme (esp. multi-Fund ones), reduction of data required in annual reports, revision of timing of data collection	• Correct assessment of EC regarding shake-up – considerable investment already made and general changes difficult due to variety of indicators/systems in place • Changes possible on bilateral MS:EC basis
Performance Reserve (PR)	• New requirement with unpredictable consequences (including political) and concern that early programme difficulties will not be sufficiently reflected • Processes (defined by MSs) sometimes very complex	• In light of proportionality, focus on selection of simplified parameters and avoidance of overly complex systems • Reduce number of indicators to 8-12 • Single decision at mid-term point on programme/PR adaptation	• Wide variation between MSs on impact of PR (full competition only in some MSs) • Principle of PR (encouraging good management) sound and EC proposals for simplification positive. Still need to address issue of whether justification/ qualification for 'under-performance' to be permitted
Annual Meeting	• Useful for EC as opportunity to influence progress but potential for duplication with Monitoring Committee meetings. Meetings insufficiently strategic and retrospective.	• Realise an effective annual review (avoid duplication, sharper strategic focus) • Greater efficiency (option for letter exchange instead of meeting, video conf.)	• Constructive suggestions from EC, particularly on option for review without physical meeting. Central objectives of annual meeting could be clarified further.
EC Role in Monitoring Committees	• Advisory role of EC and discretionary powers of MS bodies should be clarified • Number and range of meetings (including annual meeting – see above) too large	• Improved preparation of Monitoring Committee meetings, including greater EC inter-departmental coordination to increase consistency and enable binding commitments to be made • Clarify strategic objectives of meetings	• Advisory role welcomed in some MSs but lack of formal intervention on technical/ administrative issues lacking as result • Positive EC proposals, although advocacy of greater exchange of experience impractical
Financial Management	• Range of financial management issues relevant targets for simplification including n+2, part-financing rules, treatment of advances in declarations of expenditure. • Specific issues affect MSs differently – key concern is the widespread implications of n+2	• Range of technical suggestions associated with simplifying administration of n+2 rule related to eg. selection of dates, time calculations and programme amendments	• n+2 effective in encouraging financial efficiency but inhibited innovation in some programmes • Early programming difficulties suggest likely n+2 impact on high number of programmes with damaging political consequences at all levels. EC suggestions positive but may make little real difference - consideration should be given to n+3 option

Notes: MS = Member State; MSs = Member States; SF = Structural Fund; SFs = Structural Fund

8. ISSUES FOR DISCUSSION

The debate on the reform of the Structural Funds is still in its early stages. Member States have begun to highlight some of the main budgetary and organisational issues of concern, and the Commission has been promoting discussion of future development priorities. However, many of the key issues – such as the proportion of EU GDP devoted to regional policy, the treatment of Objective 1 regions subject to the 'statistical effect' or whether Structural Funds continue to provide support outside the lagging regions – will not be decided for some time. Indeed, the debate over the reform of Structural Funds is overshadowed by the potentially greater political and economic implications arising from reform of the CAP.

In this context, the debate at the Sponsors' Meeting could usefully consider some the less political issues which are nevertheless important questions in considering the future of the Structural Funds: What is the added value of the Structural Funds? And how might a new approach to Structural Funds outside the lagging regions be operationalised?

8.1 What is the 'added value' of the EU Structural Funds?

For several Member States, especially the 'net payer' countries, the added value of the Structural Funds is an important factor in their approach to the reform debate. In a situation where the financial receipts after 2006 may be relatively small, the question is whether the Funds deliver wider benefits, by virtue of the approach to implementing Community regional policy. This issue has been raised specifically by Germany, Austria and the UK, but also features in the policy debates of other Member States.

In the Second Cohesion Report, the Commission's view is that EU regional policy has several non-financial advantages[48]:

> *"The value added of Community involvement in regional development is not only related to the expenditure incurred as such. Benefits also stem from the method of implementation developed in the 1988 reform of the Structural Funds, which was revised in each subsequent programming period".*

According to the Commission, these benefits stem partly from the programming system, since the multi-annual planning process has encouraged participants to adopt a 'strategic' approach leading to better selection and greater coherence of co-financed projects. New partnership arrangements have been established to implement programmes, becoming a permanent mechanism to exchange information and experience, and encouraging more coherent policies and shared objectives. The monitoring and evaluation obligations have also improved the efficiency of programme implementation and led to more transparency and better policymaking.

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[48] CEC (2001b) *op. cit.*

There is considerable evaluation research to support the fact that, over time and across most Member States, the implementation of the Structural Funds has improved. Since the first programming period (1989-93), there has been a progressive increase in positive and pro-active compliance with the principles of programming and partnership and the requirements for monitoring and evaluation. In the latest generation of programmes (2000-06), the implementation of many regional development strategies is based on relatively sophisticated systems for managing and monitoring the allocation of resources.

What is less clear is whether this approach to implementing the Funds can be said to comprise added value in the sense that it leads to the quality or quantity of economic development being greater than it otherwise would have been in the absence of EU regional policy. For some Member State policymakers, the reverse would apply for three reasons. First, the policy priorities of the Structural Funds (or the way that they are interpreted) are said to 'distort' national policy spending objectives by requiring co-financing on areas of intervention or types of project that are not necessarily the preferred options of Member State authorities. Second, the institutional approach to implementing the Funds does not necessarily accord with national practices. Third, as noted above, the implementation of the Structural Funds requires the commitment of major administrative resources at both national and regional levels, which can be regarded as disproportionate to the volume of assistance.

Until now, there has been no objective assessment of the 'added value' of the Structural Funds. The Commission has recently attempted to provide a methodological approach for evaluating Community added value, with a view to justifying structural policies at Community level. The concept is defined as[49]:

> *"the value resulting from the Community assistance which is additional to that which would have been secured through the Structural Funds and the Cohesion Fund by the national and regional authorities and the private sector. In other words, it is an assessment of the economic and non-economic benefits associated with cohesion policy as a whole and with each of the programmes implemented in the eligible regions".*

The problem with the Commission's methodology, as the German Ministry of Finance has pointed out[50], is that it does not adequately separate out those effects that would be induced by regional policy anyway (regardless of whether organised at EU or national levels) from the additional effects that are specifically attributable to the implementation of the Structural Funds. In other words, it would not be able to demonstrate that the EU implementation system is more effective than the systems of the Member States. The same applies to virtually all Structural Fund evaluations, whether carried out by the Commission or Member State authorities; they generally

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[49] CEC (2002) *Community Added Value: Definition and Evaluation Criteria*, Working Paper, DG Regio, Commission of the European Communities, Brussels.

[50] BMF (2002) *Stellungnahme zu dem von der Kommission im Januar 2002 vorgelegten Arbeitspapier "Der Mehrwert der Gemeinschaftspolitik im Rahmen der Strukturpolitik*", Federal Ministry of Finance, April 2002.

examine the efficiency and/or effectiveness of the Structural Fund implementation system but not distinguished from national policy influences.

A preliminary attempt has been made in the UK to determine whether the added value of the Structural Funds can be analysed.[51] Unsurprisingly, quantification of added value is inhibited by significant methodological problems, notably the absence of a counterfactual, and the difficulty in demonstrating causality. However, there is some qualitative evidence of the positive and negative effects of the Structural Funds on national policymaking processes – in areas such as strategy development, partnership, rationality in resource allocation and engagement of the private sector – but this would need more in-depth investigation to be used as a basis for future EU regional policy.

It may, therefore, be necessary to accept that analysing the 'economic added value' of the Structural Funds is not possible and that the key issue is 'political added value' As noted in the Austrian contribution earlier[52], this implies justifying the Structural Funds in terms of making the benefits of European integration visible to citizens or as an incentive to stimulating innovations in regional policy.

8.2 How might a new approach to Structural Funds outside the lagging regions be operationalised?

In the earlier discussion of Member State perspectives, it was noted that some countries have suggested that the post-2006 Structural Funds should be restricted to lagging regions or poor countries. Others have put forward arguments that EU regional policy should continue to have a role outside Objective 1 for a mix of economic and political reasons. If Objective 2 (or 3) does continue, it may be in a different form, recognising the range of development priorities and interests competing for support. Among the possible implementation systems for future EU regional policy action outside the lagging regions, one option is for a simple budgetary transfer to the Member States, another is for a variant on the 'status quo'. The alternative currently being considered is the 'menu approach' although, as yet, it is unclear how this might be operationalised.[53]

A starting point is to consider the ***priorities*** on which non-Objective 1 support might be focused. The Commission has put forward a range of spatial priority areas (urban areas, rural areas in difficulty, industrial areas undergoing conversion, areas with geographical or demographic handicaps) as well as two thematic priorities (the new

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[51] Bachtler J, Fraser A, Raines P and Hearns D (2002) *A Feasibility Study for an Evaluation of the impact and Added Value of the EU Structural Funds in the UK*, Report to the UK Department of Trade and Industry, European Policies Research Centre, University of Strathclyde, Glasgow.

[52] Huber W (2002) *op. cit.*

[53] Some preliminary consideration has been given to this issue by the EC 'Forward Studies Advisory Group' (minutes of meeting of 27 February 2002) and in a personal paper by Sture Åstrom (Ministry of Industry, Employment and Communications, Sweden), *Next programming period – regions in conversion or confronted with specific difficulties – a personal note,* 13 February 2002.

economy and information society and sustainable development) and networking. A variant on this approach would be to make the specification of priorities at Community level exclusively thematic, linking EU regional policy action more directly to the Lisbon agenda (see box below).

The Lisbon Agenda for Employment, Economic Reform and Social Cohesion

- An information society for all: improving access to communications infrastructure, especially among excluded groups; using information technologies to renew urban and regional development and promote sustainable development
- Establishing a European area of research and innovation: improving the efficiency and innovation of research activities; improving the environment for research
- Creating a business friendly environment for SMEs: encourage the key interfaces between companies and financial markets, R&D and training institutions, advisory services and technological markets
- Education and training for living and working in the knowledge society: development of local learning centres, promotion of new basic skills
- More and better jobs: improving employability and reducing skills gaps; encouraging lifelong learning; reducing deficits in the service economy; extending equal opportunities
- Promoting social inclusion: improvement of skills; promotion of wide access to knowledge and opportunity

These objectives could provide a basis for establishing the development priorities for Structural Fund intervention. However, given that Member States already have policies in operation to address these kinds of objectives, it would arguably be necessary to establish some accompanying principles to ensure the effective use of the Funds, such as :

(a) additionality – improving the effectiveness or efficiency of economic development;
(b) innovation – promoting experimentation, learning, risk-taking, the exploitation of new ideas in economic development
(c) visibility – ensuring that EU intervention is visible to local communities and individuals.

A second question concerns the mechanisms for ***allocation of the Funds***, which hitherto has had a financial and spatial component. In determining allocational issues, the EU would need to take account of the political dimensions of the allocation process, the potentially small amounts of funding involved, relative to the current programmes, and the experience of spatial targeting outside Objective 1 areas. One of the most straightforward approaches could be to distribute a financial allocation to each Member States on the basis of simple criteria such as GDP per capita, supplemented by a labour market and/or geographical criterion. The Member State

would then be able to distribute the financial allocation to regions, either using the same EU-level criteria or its own allocation system. Spatial targeting could take one of several options:

- *Option 1: Spatial targeting at EU level.* The European Commission determines the criteria for spatial targeting of the Structural Funds, either with common indicators for all Member States or by providing a menu of indicators from which Member States can make a selection, with the resulting maps being adopted by the Commission. This would ensure consistency and coherence of Structural Funds area designation across the EU and provide a possible basis for coherence between Structural Fund and national regional aid maps (although there are mixed views as to whether this is desirable). However, there is a limited range of EU-wide comparative indicators, especially given the narrow spatial targeting implied by parts of the Commission’s suggested menu of priorities. An EU-level approach also has the potential for incoherent or illogical map outcomes at regional or local levels, and is not able to take account of region-specific needs.

- *Option 2: Spatial targeting at Member State level.* Member States determine the criteria for the spatial targeting of Structural Funds, designating the maps according to national indicators. This would respect the principle of subsidiarity, allow Structural Funds to be adapted to national policy requirements and facilitate consistency/coherence between Structural Fund and national regional aid maps. On the other hand, there would be inconsistencies in area designation and maps across the EU. Moreover, this approach may only be able to take limited account of region-specific needs.

- *Option 3: Spatial targeting at regional level.* The spatial targeting is carried out at regional level, with regional authorities selecting the criteria to be used within parameters (indicators, ceilings, systems) established at Member State level. This approach would reflect the regionalisation of economic development policy evident in many EU Member States and allow Structural Funds to be focused on region-specific needs. On the other hand, there would again be inconsistencies in area designation across the EU potentially within as well as between Member States and it would be difficult to enforce the principle of the concentration of aid. Greater onus would be placed on the regional level to comply with State aid rules, which might cause problems for national governments in exercising their responsibility for State aid compliance.

- *Option 4: No explicit spatial targeting.* A more radical option would be for Structural Fund support to be allocated at regional level on the basis of ‘implicit’ spatial criteria (eg. reducing digital exclusion in disadvantaged communities). Rather than creating boundaries on the basis of statistical criteria, which by their nature are arbitrary, a ‘bottom up’ system could be conceived whereby the targeting of the support is adapted to suit the needs of individual measures or even projects. This would potentially provide maximum flexibility in the allocation of aid but would be highly complex to administer and create uncertainties in administration for policymakers, programme managers and applicants. As with the previous option, it would be difficult to enforce the principle of concentration and would create difficulties in ensuring compliance with State aid rules.

The final question concerns the ***implementation system***. In accordance with the requirements for simplification and decentralisation, the Commission would have to be minimally involved in the implementation process, enabling the Funds to be managed and delivered in accordance with Member State systems and procedure. This could imply a system along the following lines[54]:

- the Commission and Member State would agree a regional development contract stipulating the development priorities selected by the Member State (from a list or priorities laid down in the Regulations), specifying the outputs to be achieved, the conditions for receipt and evaluation of the support, and statements of compliance with Community policies;

- the Member State would be responsible for implementation, including ensuring effective systems for monitoring, financial control and auditing; and

- the Commission would be responsible for evaluation of assistance and for validating the quality of national systems for financial control.

Such a system would potentially address the concerns of those Member States most concerned at the complexity of the Structural Funds and the desire for any post-2006 assistance outside Objective 1 to be simple to administer and decentralised to national level. However, it would run counter to the practice hitherto of having a standard implementation system for all types of Structural Fund programme and create two distinct categories of administrative system. It would also be difficult for the Commission to ensure that concentration of assistance was being achieved and that financial control and audit was being effectively carried out, especially given the current incidence of fraud and the (growing) number of irregularities in the administration of the Funds. Nevertheless, if Member States were prepared to comply with the principles of additionality and innovation in the use of the Funds, such a system could deliver real added value for regional development.

Acknowledgement*: The authors are grateful to Martin Ferry, Laura Polverari and François Josserand for their research assistance in preparing this paper.*

[54] Adapted from Åstrom S (2002) *op. cit.*