EU BUDGET PRIORITIES, EXPENDITURES AND RESOURCES

EU Budget Reform and the New Low-carbon Economy

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If Member States are to address the collective challenges threatening their security and prosperity, an effective European Union (EU) budget is imperative. In June 2011, the European Commission will publish its proposals for the next Multiannual Financial Framework (MFF). Given that the size of the EU budget is unlikely to increase, the quality of spending becomes ever more important, with pressure building for a more active prioritisation in line with the current and future strategic EU goals identified in the Europe 2020 Strategy. This chapter argues that low-carbon investment must lie at the heart of the next EU budget.

A new narrative for EU climate policy

We are witnessing a shift in perceptions about how the EU should address the challenge of climate change. While the ultimate end goal of securing a stable climate remains the same, a more hard-headed calculation of European self-interest is driving thinking on the benefits of moving to a new low-carbon economy. Gone are the days when an appeal to "international leadership" could form the central motivating theme for EU climate policy.

The European Commission's February 2011 Communication on a "Roadmap for moving to a competitive low-carbon economy in 2050" indicates that the economic recession has resulted in a reduction in the costs of policy action, together with a range of positive co-benefits to the European economy, such as those linked to reductions in fossil fuel imports. Independent analyses further point to the improved distribution of costs and benefits to the European economy resulting from early efforts to reduce emissions, rather than delaying action into future decades, which risks locking-in high carbon patterns of investment.[1] Similarly, the recent study "A new growth path for Europe: generating prosperity and jobs in the low-carbon economy" highlights that, if learning dynamics and investor perceptions are incorporated into modelling assumptions, a 30% emissions reduction target for 2020 could result in increased economic growth and reduced unemployment.[2]

The challenge facing EU decision makers is therefore to create a set of interlocking policy drivers that increase investments in the technologies and infrastructures that will make the shift to a low-carbon economy possible. These policies must have a "robust credibility" if they are to succeed. The European Commission estimates that per annum, an additional €270 billion of public and private investment is needed between 2010 and 2050 compared to business as usual scenarios, with the increase in the period 2014-2020 being less pronounced, reflecting the time-lag between investment plans and actual spending.[3] This figure represents added investments of about 1.5% of total annual EU Gross Domestic Product (GDP) and amounts to more than twice the size of the current annual EU budget (approximately €120 billion).[4] It is within this context that we can view the potential added value of the EU budget, not as the sole delivery vehicle for investment on this scale, but as a catalyst to orientate many other spending decisions.

Why the EU budget matters

As a political signal of the EU's collective will to move towards a low-carbon economy, the EU budget is unparalleled, in that it will provide the most visible demonstration of the EU's policy priorities for the remainder of the decade. As a policy instrument, it can leverage investment and incentivise policy delivery in ways that complement the impact of carbon pricing and regulatory approaches. It is the tangibility of EU budget decisions that accounts for its influence, for citizens, private sector investors, and Member States alike:

For citizens, public spending is understandable on a personal level due to its parallels with their own lived experience, something that cannot be said of more esoteric challenges such as "saving the euro". In an age of austerity within national politics, and increasing scepticism of the value of EU cooperation, it is an imperative for the EU budget to demonstrate that it is not being wasted, but instead is being visibly invested to fuel future low-carbon growth.

For private sector investors, the multiannual nature of the EU budget can help provide the policy credibility and durability required to unlock investment. There is an international component to this too, in that a concerted effort to catalyse national and regional low-carbon

1. See for example Emmanuel Guerin, "Is there a case for the EU moving beyond 20% GHG emissions reduction target by 2020?", Climate Strategies, 2011, available at: http://www.climatestrategies.org/research/our-reports/category/57/312.html
2. Carlo C. Jaeger et al., "A New Growth Path for Europe: Generating Prosperity and Jobs in the Low-Carbon Economy. Synthesis Report", European Climate Forum, 2011, available at: http://www.european-climate-forum.net/fileadmin/ecf-documents/Press/A_New_Growth_Path_for_Europe__Synthesis_Report.pdf
3. European Commission, Communication, "A Roadmap for moving to a competitive low carbon economy in 2050", COM(2011) 112 , 8 March 2011, available at: http://ec.europa.eu/clima/documentation/roadmap/docs/com_2011_112_en.pdf
4. *Ibid.*

development strategies via the EU budget will provide an improved level of assuredness for international capital providers, while simultaneously boosting the EU's collective position *vis-à-vis* the rapidly increasing low-carbon investments underway in China and other emerging economies.[5]

For Member States, the EU budget can play a catalytic role in fostering improved political receptiveness towards investment in the new low-carbon economy. Despite the emerging framing for EU climate policy discussed above, the question remains as to how to make this new low-carbon economic model an attractive proposition for all Member States. Proponents of a "low-carbon transition" for Europe must bear in mind that Central and Eastern European (CEE) Member States have already been through an enforced "low-carbon transition" of their own, and that, for many of their citizens, it was a miserable experience. EU climate policy has already sought to address this through decisions on effort sharing and flexibilities within the emissions trading system, yet more will need to be done to address CEE Member States' understandable hesitance.

For all three of these audiences, the EU budget can play a pathfinder role by fostering an explicitly pro-investment, pro-growth approach to stimulating a new low-carbon economy. The central success criteria for the leaders of the European institutions must therefore be that they secure an EU budget that clearly invests in meeting Europe's current and future challenges, not continuing to spend money reflecting past political compromises.

The 2008 consultation on the budget review identified climate, energy and competitiveness as the top three priorities for the next EU budget, and that prioritisation still holds true today, notwithstanding the immediate short-term pressures of the economic crisis. Given that previous MFF periods have been communicated under the narratives of "Single Market", "enlargement" and "Lisbon Agenda", we would therefore propose that this next MFF should be presented as one of "investing in the future" via catalytic spending on low-carbon infrastructure and innovation. Clear conditionality mechanisms will be required to ensure that low-carbon outcomes result as headline MFF decisions flow down into programming frameworks and Member State prioritisations.

Making up for a missed opportunity

The reality check for supporters of reform is that the history of the EU budget provides a potent demonstration of the EU's struggle to align political will and economic resources behind the pursuit of its policy priorities. Member State negotiating strategies are driven primarily by *juste retour* calculations of net benefit or loss rather than a consideration of policy outcomes, while negotiations additionally suffer from conflicting policy aims within

5. Pew Environment Group, "Who's winning the clean energy race? 2010 Edition", 29 March 2011, available at: http://www.pewenvironment.org/uploadedFiles/PEG/Publications/Report/G-20Report-LOWRes-FINAL.pdf

and between Member States. These dynamics are likely to be further reinforced in 2011-12 by the impact on public finances of the current economic downturn.

Additionally, we must include in this inauspicious mix the missed opportunity of the Budget Review process agreed at the time of the last negotiations in 2005, but not delivered by the Commission as intended during 2008-09. The Commission's forthcoming MFF proposals are subsequently expected to start from a position much closer to the status quo, rather than incorporating novel ideas such as the "climate and energy axis" included in the leaked draft Budget Review paper of October 2009.[6] Notwithstanding the reduced scope for a radical revision of budget structures, the Commission will still need to communicate a clear political narrative and include strong policy instruments to deliver low-carbon outcomes. With a mainstreaming approach expected, the pressure is now on to identify how the next MFF will deliver a prioritisation of resources.

Given the expectation that cohesion funds will continue to be accessible to all regions of the EU, a strong case can be made for climate and energy actions to form the leading priorities for investment, requiring both a prioritisation of low-carbon outcomes, and an effective "climate proofing" approach that reduces lock-in to higher-carbon spending and identifies win-win opportunities to catalyse next generation infrastructures.[7] There is therefore an implicit deal that will need to be reached during the MFF negotiations, whereby CEE Member States secure the resources they desire for Cohesion policy in return for a clear commitment that a significant portion of these funds will be dedicated to investments that support the development of the low-carbon economy.

Similarly, spending on the Common Agricultural Policy should match the overarching "investment" narrative by being oriented towards ecosystem and biodiversity protection and rural development. Likewise, funding for research and development (R&D) and critical infrastructures will need to prioritise the broad set of investments that can help stimulate a low-carbon economy, including broadband internet, digital services, energy infrastructures and transportation technologies. Proposals for a new system of EU project bonds and the further development of innovative financial instruments could both play useful roles in catalysing spending, provided that they too are subject to the same low-carbon objectives.

Such measures taken within the current budget framework would result in a surge in spending on climate, energy, environment, and a broader suite of technologies and infrastructure compatible with the low-carbon economy, up from the current level of direct spending on the environment, which today equates to just 5-8% of the total multiannual EU budget. Recent analysis

6. European Commission, leaked draft communication, "A Reform Agenda for a Global Europe [Reforming the Budget, Changing Europe]", October 2009, available at: http://lowcarbonbudget.eu/timeline/european-commission/the-leaked-draft-budget-review-communication/
7. Keti Medarova-Bergstrom et al., "Strategies and instruments for climate proofing the EU budget", Institute for European Environmental Policy, 2011, available at: http://www.ieep.eu/assets/782/Climate_proofing_EU_budget.pdf

by the World Wildlife Fund suggests that 43% of the total EU budget could play such a positive role.[8] Assuming a stable multiannual budget in relative terms (1.13% of EU Gross National Income) for the next MFF, this would translate to €492 billion over the 2014-2020 period. A prioritisation of low-carbon outcomes from a third or more of the EU budget would provide a clear demonstration of political intent, particularly if coupled with some specific low-carbon wins such as investment in the Strategic Energy Technologies (SET) Plan.

Conclusions: Member State champions required

It is difficult to imagine that the EU will be on track to a low-carbon economy in 2020 if the next EU budget is not clearly aligned with the promotion of low-carbon outcomes as a driver for private sector investment. Similarly, there is a need for a popular mobilising focus that can engage different stakeholder interests and Member State coalitions in a collective effort to secure a future-oriented budget. Such a mobilising focus must encompass a range of national and sectoral interests, while being sufficiently clear that it can redirect spending patterns within the EU budget in reality and not just on paper. We believe that the pursuit of a low-carbon agenda can provide this motivating force.[9]

Ultimately, low-carbon outcomes will only be secured from the next MFF if Member States make these a priority in the negotiations. Such outcomes are however already at risk in that ministries of environment or energy are not the lead departments in the sectoral negotiations. To mitigate this, there need to be joint positions within governments and high-level support to ensure low-carbon outcomes are not side-lined. One example of how this can be pursued is the United Kingdom's (UK) position detailed in its March 2011 Carbon Plan, which gave the UK Treasury the task to: "Complete negotiations on next EU budget spending period – including agreement to increase the share of EU budget allocations for low-carbon investments within a reprioritised budget."[10]

There of course remains the risk that this aim will be overtaken by the UK's traditional priorities of a small budget and maintenance of its rebate, but the public statement of this position gives leverage to external stakeholders to hold the UK government to account for the final budget deal reached. The best chance of success will come via the development of coalitions of Member States who share an interest in low-carbon outcomes, and who can agree that they provide a means of improving the quality of spending of the EU budget. Usefully, this interest already cuts across the traditional categories of net-contributor / net-recipient, with Member States such as Greece, Portugal and Spain all championing the push for a 30% emissions reduction target for 2020.

Recommendations

European Commission. One of the central criteria against which Commission President José Manuel Barroso's time in office will be judged will be his ability to deliver a future-focused budget that reflects his "no taboos" rhetoric. The Commission must set the tone for the MFF negotiations via proposals that present the EU budget as an investment in Europe's future, accompanying this with clear conditionality mechanisms. The headline narrative must be further demonstrated with some iconic wins such as funding for the Strategic Energy Technologies (SET) plan. An approach that relies on mainstreaming alone will not be sufficient.

Council Presidencies. The majority of the negotiations are envisaged for the Polish and Danish Presidencies. Despite their different positions on either side of the net- recipient / net-contributor divide, they do share a concern for a broader approach to European economic recovery beyond eurozone governance, and were both signatories to the letter from nine heads of state and government to Presidents Herman Van Rompuy and Barroso in March 2011 that included a call for "an EU budget which addresses the challenges of tomorrow". They will need to maximise the scope for prioritisation of low-carbon policy outcomes, not allowing them to be squeezed out of sectoral formations or dropped from the political negotiations when the going gets tough.

Member States. Member States themselves will need to develop their own internal strategies that join-up across ministries, identifying opportunities for low-carbon spending and modalities for policy delivery. Ministries of environment, climate and energy will need to provide consistent internal pressure to ensure measures such as "climate proofing" are maintained. As the negotiations proceed, coalitions of Member States will be required to ensure that low-carbon outcomes are secured and clearly communicated. Just as previously the "friends of Cohesion Policy" coalition did much to shape the final outcome, this time around there will need to be a "friends of low-carbon investment" group.

External stakeholders. Decisions on the next MFF will ultimately be taken by heads of state and government at the European Council. Domestic political pressure from civil society and private sector in favour of investment in the low-carbon economy will therefore be of value, particularly if framed as the key success criteria against which the final deal will be judged. There is therefore a need for a smart mobilisation of influence in support of budget reform proposals, as a counterbalance to the pressure from existing vested interests. The EU budget negotiation offers the best opportunity in the next two years for sustained political influence. We should seize it.

8. Sebastien Godinot, "Unlocking the potential of the EU budget – Volume 2: Intelligent Investments", World Wildlife Fund – European Policy Office, March 2011, available at: http://www.wwf.dk/dk/Service/Bibliotek/Handel/Rapporter+mv./Unlocking+the+Potential+of+the+EU+Budget+vol+2
9. See for example the contributions from private sector, NGOs, social groups and think tanks in Green Alliance's 2010 publication: Chris Littlecott (Ed.), "Unlocking a low-carbon Europe: perspectives on EU budget reform", 2010, available at: http://www.green-alliance.org.uk/uploadedFiles/Publications/reports/unlocking_a_low-carbon_Europe.pdf
10. David Cameron, Nick Clegg and Chris Huhne, "Carbon Plan", Department of Energy and Climate Change (DECC), HM Government (UK), 2011, p. 61, available at: http://www.decc.gov.uk/assets/decc/What%20we%20do/A%20low%20carbon%20UK/1358-the-carbon-plan.pdf