EUROPEAN COMMISSION

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Dear President,

The Commission would like to thank the Bundesrat for its Opinion on the proposal for a Regulation of the European Parliament and of the Council on the European Regional Development Fund and on the Cohesion Fund {COM(2018) 372 final}.

The proposal forms part of a broader package of ambitious measures designed to govern cohesion policy for the post-2020 period and to promote socio-economic and territorial cohesion across the European Union. On 2 May 2018, the Commission adopted a proposal for the next Multiannual Financial Framework for 2021-2027 for investing where it matters. On 29 May 2018, it adopted a proposal for a Regulation laying down common provisions on the European Regional Development Fund, the Cohesion Fund and five other funds {COM(2018) 375 final}.

The proposal aims to define fund-specific rules for the use of the European Regional Development Fund and the Cohesion Fund post-2020. The Commission welcomes the Bundesrat's broad support for the aims of the proposal, but notes its doubts relating to a series of issues. The Commission is pleased to have this opportunity to provide a number of clarifications regarding its proposal in the Annex.

Discussions between the co-legislators, the European Parliament and the Council, on the proposal are now underway and the Commission remains hopeful that an agreement can be reached in the near future.

Yours faithfully,

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First Vice-President

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Annex

The Commission has carefully considered the issues raised by the Bundesrat in its Opinion and is pleased to offer the following clarifications, grouped by topic.

Simplification

The Commission is convinced that it has tabled a whole series of important simplification proposals (not only in the proposal on European Regional Development Fund and Cohesion Fund, but mainly in the proposal for Common Provisions Regulation) and simplified the conditions for the programming period 2021-2027 in a number of ways.

Just to give – amongst others – three examples for what the Commission proposes:

Firstly, the proposed simplified cost options alone could save up to 20-25% of administrative costs for programme managers. Apart from the traditional reimbursement based on real costs, the Commission also opened the possibility to use financing not linked to costs as one of the forms of Union contribution.

Secondly, the Commission eliminated the time-consuming and complex process of major projects appraisal. The designation process as well as the specific rules for revenue-generating projects were removed as well.

Thirdly, the ex-ante evaluation of programmes will no longer be obligatory.

For a full list of all 80 proposed simplifications, please refer to the Commission's "Simplification Handbook"[1].

Thematic concentration

The Commission takes note of the Bundesrat's concerns regarding the high levels of thematic concentration for policy objectives 1 and 2, and that this concentration is defined at national (rather than regional) level.

Thematic concentration means the European Union is able to ensure that cohesion policy is focused on European priorities. Innovation and a low-carbon economy are both crucial for the Union's competitiveness and to help adjusting structurally to globalisation pressures and challenges, thus the high concentration on policy objectives 1 and 2 reflect the high priority within the European Regional Development Fund for the transition to a smarter economy and to a low-carbon economy. It makes sense for the

[1] *http://ec.europa.eu/regional_policy/en/information/publications/factsheets/2018/simplification-handbook-80-simplification-measures-in-cohesion-policy-2021-2027*

European Union to concentrate its spending on these areas – especially in the richer Member States, where allocations are in any case lower and critical mass of investment more important. That is why the Commission proposes to keep concentration, but to make it clearer and simpler to programme and implement. The final say on the application of the thematic concentration methods in programmes will be a matter of discussions between the Commission and the Member States.

When it comes to the high levels of concentration for policy objectives 1 and 2, the Commission would like to point out that it is mainly through thematic concentration that cohesion policy resources are prevented from being spread too thinly. The greatest risk is obviously in richer countries where the allocation per head is smallest, hence the higher requirements. Policy objectives 1 and 2 encompass a very broad range of activities, ranging from research and innovation to enhancing the competitiveness of small and medium-sized enterprises, skills, digitalisation, energy efficiency, circular economy, environment and climate change adaptation. There is still plenty which can be done in richer countries. In addition, large investments in e.g. infrastructure are less appropriate in rich regions and should be confined to duly justified cases.

However, the higher concentration requirements for policy objective 1 and policy objective 2 go hand in hand with a greater flexibility given to Member States to organise their programmes accordingly. This approach in fact recognises the difference in administrative organisation of different Member States as well as different needs and potential of different regions. With the thematic concentration requirements defined at national (rather than regional) level, it is for each Member State to find the right mix for the different needs of its regions.

The Bundesrat also voices objections as to the use of both Gross National Income (at national level) and Gross Domestic Product (at regional level) as indicators for allocations. Gross National Income includes income earned abroad. It is therefore the fairest measure of a nation's capacity to pay – which is why the Commission uses it to determine co-financing, as well as the national component of allocations. On the other hand, Gross Domestic Product, by not including income earned elsewhere, is the best measure of actual economic activity in a region – therefore the best measure of the level of development in that region. For these reasons, it is a longstanding practice in cohesion policy to use Gross National Income at the national level and Gross Domestic Product at the regional level.

Scope of support

Financial support to large enterprises is excluded for productive investments (unless they cooperate with small and medium-sized enterprises). Large enterprises (often state owned or with large public stake) may benefit from investments in infrastructure. Ex post evaluations of cohesion policy have shown significant deadweight effects for cohesion policy support to large enterprises: in many cases, the European Regional Development

Fund support provided was not the decisive factor for a large enterprise to carry out an investment, and many of these investments would most likely have taken place also in the absence of the European Regional Development Fund support. Large enterprises normally have better access to finance, as they have more collateral and involve fewer risks. Where Member States feel such public support makes a crucial difference, they are of course free – within the applicable state aid limits – to provide it through national funding, but this is not a priority for the European Regional Development Fund. The latter focuses its support on small and medium-sized enterprises which clearly have more difficulties regarding access to finance and which are the main source of job creation.

With regard to future <u>*support to small and medium-sized enterprises*</u>*, the Commission emphasizes that one of the big political priorities of the European Union post-2020 is research and innovation (cf. its proposal to significantly increase the budget for Horizon). Cohesion Policy has to factor this in and that is why the Commission is embedding future small and medium-sized enterprises support and skills development under policy objective 1 "a smarter Europe by promoting innovative and smart economic transformation". While the codes for the types of intervention foresee also more generic activities ("Business infrastructure for small and medium-sized enterprises (including industrial parks and sites)", "small and medium-sized enterprises business development and internationalisation"), most of them are linked to innovation-driven investments, and also the (common output and result) indicators clearly reflect the focus on research and innovation. In any case future support to Small and medium-sized enterprises will have to take place in the context of a Smart Specialisation Strategy. Having in place such a strategy is a thematic enabling condition and therefore support measures for the policy objective "Smarter Europe" will have to serve the implementation of such a strategy.*

On the notion of "<u>*undertakings in difficulty*</u>*" and financial instruments' support to start-ups: the exclusion of European Regional Development Fund and Cohesion Fund financing for undertakings in difficulties was already present in the 2014-2020 regulations. The aim of such exclusion is to ensure that investments are focused on enterprises that are in the best position to contribute to the creation of growth and jobs. The change for the post-2020 period consists in the fact that the notion of "undertakings in difficulties" is better defined. In the 2014-2020 period, the provisions referred to "undertakings in difficulties as defined in Union State aid rules". For the post-2020 period, reference is made to the precise definition as contained in the General Block Exemption Regulation. This clarifies that the notion of "undertakings in difficulties" does not exclude start-ups from receiving European Regional Development Fund (and Cohesion Fund) support, on the basis that these would by their very nature be "in difficulties" as they are only starting their activities and may thus be struggling to establish themselves on the market and have access to financing.*

The Commission has proposed the exclusion from the scope of the European Regional Development Fund and the Cohesion Fund of investment in <u>*disposal of waste in landfill*</u>*. In 2018, a new landfill reduction target (of 10% by 2035) was introduced in Union law, to prevent detrimental impacts on human health and the environment and to ensure that* *economically valuable waste materials are recovered through proper waste management. In this context, it goes without saying that European Union funds should not contribute to supporting investment in landfills, which will progressively have to be phased out, but to provide incentives for reusing, recycling or recovering valuable materials.*

The Commission has also proposed the exclusion from the scope of the European Regional Development Fund and the Cohesion Fund of investment in <u>facilities for the treatment of residual waste</u>. Since 2008 already, EU waste policy follows a hierarchy of measures in the following priority order: prevention, preparing for reuse, recycling, recovery (including energy recovery) and disposal. The treatment of residual waste includes operations of low added value at the bottom of the waste hierarchy, such as mechanical-biological treatment, incineration and landfilling. Furthermore, the revised Waste Framework Directive calls for ambitious recycling targets of 55% and more for 2025 and beyond. Investing in new treatment facilities can lead to structural overcapacities and to infrastructures that rely on a constant influx of unrecycled waste for decades to come. This disincentivises recycling, creates a lock-in and prevents Member States from reaching their recycling targets. Instead, cohesion policy will seek to support a successful transition to the circular economy, notably by adopting a long-term perspective and focusing investment on prevention, preparing for reuse and recycling. Those Member States that still have the need for infrastructure for the treatment of non-recyclable waste, as justified in their updated Waste Management Plans, could still use national or other funds for this.

Funding for the purchase of <u>rolling stock</u> for use in rail transport is also excluded from European Regional Development Fund and Cohesion Fund support (under certain conditions). The 4th Railway Package, adopted on 14 December 2016, introduces the principle of competitive tendering of public service contracts in rail transport. As from December 2019, Member States' competent authorities shall award public service contracts based on competitive tendering procedure, with a derogation period running until 24 December 2023. After that date, an unconditional direct award of public service contracts in rail will not be possible. Rolling stock funding today will have long lasting effects on market access conditions due to their long lifetime (30-35 years). Therefore, rolling stock procurement shall not jeopardise the foreseen market opening in rail passenger services by providing an unfair competitive advantage to incumbents.

<u>Climate protection</u>

Regarding the <u>30% objective</u> for the European Regional Development Fund budget's contribution to climate change objectives, in light of the experience with current implementation and the expected increase of expenditure for climate change objectives (given the thematic concentration for policy objective 2), the Commission is very confident the 30% target will be met. The weighting of categories in Annex I of the *proposal for Common Provisions Regulation has been largely maintained to ensure continuity and comparability across programming periods.*

The Commission fully recognises the important contribution that <u>promoting sustainable multimodal urban mobility</u> (Art. 2(1)(c)(IV)) makes to the achievement of the Union's climate change objectives. Moving this from policy objective 3 to policy objective 2 would weaken thematic concentration under policy objective 2 though, at the expense of other types of investments and specific objectives foreseen under policy objective 2. The Commission has therefore deliberately included this type of intervention under policy objective 3, "a more connected Europe by enhancing mobility and regional information and communication technology connectivity".

<u>*Integrated urban development*</u>

Urban earmarking is based on the particular focus of the territorial strategy on urban areas. It does not favour any specific territorial tool. As specified in Annex I, proposal for Common Provisions Regulation, on the types of intervention (table 3 specifying codes for the territorial delivery mechanisms) it might be an integrated territorial investment (ITI), community-led local development (CLLD) or <u>other – national – territorial tool</u> focused on urban neighbourhoods, cities, towns or suburbs or functional urban areas. Such other tools can literally be any other tools, partly already in place in various Member States, and different from integrated territorial investments. The Commission does not think that these tools de facto need to be integrated territorial investments or need to meet all the integrated territorial investment requirements. There is a much higher degree of freedom in choosing such tools.

Under the <u>European Urban Initiative (EUI)</u>, all three proposed strands are to be combined in a single framework implemented under direct or indirect management by the Commission (Art. 10) The single framework will ensure conditions for creating an effective value chain between the three strands and a better articulation between the relevant outputs of the European Urban Initiative and investments in mainstream programmes and the implementation of Urban Agenda for the European Union actions. This way, the Commission would be the best placed to upscale policy recommendations and proposals at Union level (better regulation objectives and a bottom-up approach) and ensure mainstreaming of these into other Union's policies and cohesion policy in particular. Within shared management, the Commission will not be in such a position to facilitate these processes. The objective is to free Member States from administrative burdens but at the same time keep them involved on strategic decisions. The Commission is well aware that managing authorities of cooperation programmes in the European Union and their technical secretariats in particular have acquired valuable experience over the last years. Indirect management presents the advantage of building a bridge to this knowledge.

The Commission takes note of the Bundesrat's rejection of the planned limitation of support for biodiversity and green infrastructure measures to the urban environment (Art. 2(1)(b)(vii)). It also fully acknowledges that, indeed, the preservation of biodiversity and the functionality of ecosystems also concern rural areas. Confining this to the urban environment in the proposal for European Regional Development Fund and Cohesion Fund has only been done for reasons of demarcation vis-à-vis the European Agricultural Fund for Rural Development: supporting biodiversity and green infrastructure in rural areas should be the responsibility of the European Agricultural Fund for Rural Development, not of the European Regional Development Fund and Cohesion Fund.

Indicators

The monitoring of progress in the implementation of 2021-2027 programmes will ensure more robust data thanks to a revised and more complete set of common European Union indicators. The data will be updated more frequently by the Member States and feed into the Open Data Platform in order to share the data with the wider public. The approach to indicators across all policies will be harmonised, which should allow for a clearer presentation of the cohesion policy's contribution to the wider Union objectives. The common result indicators can be aggregated and tracked for the European Union as a whole.

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