EUROPEAN COMMISSION

Brussels,19.3.2019
C(2019) 1709 final

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 laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument {COM(2018) 375}.

The proposal, adopted on 2 May 2018, forms part of a broader package of ambitious measures designed to govern cohesion policy for the post-2020 period and to promote social, economic and territorial cohesion across the European Union.

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 on the proposal will be reached in the near future.

The Commission looks forward to continuing the political dialogue with the Bundesrat in the future.

Yours faithfully,

Frans Timmermans
First Vice-President

Corina Creţu
Member of the Commission

Mr Daniel GÜNTHER
President of the Bundesrat
Leipziger Straße 3 - 4
10117 BERLIN

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 and simplified the conditions for the programming period 2021-2027 in a number of ways. The main areas for simplification include: a) extended options for simplified cost options and financing not linked to cost schemes; b) verifications, control and audit arrangement building on the single audit principle and introducing an enhanced proportionate system, and c) simplification related to programming and implementation aspects including less and streamlined qualitative reporting and evaluation requirements.

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

Regarding delegated acts it is to note that in the Common Provisions Regulation, for the period 2014-2020, there are 49 empowerments for the Commission to adopt rules on certain topics in the form of delegated regulations or to establish uniform conditions or implementing rules. The Commission is proposing nine such empowerments for the post-2020 period. This means a radical change in terms of additional rules. Moreover, these post-2020 empowerments hardly add new rules but rather focus on keeping the possibility to add new options for flexible reactions for Member States during implementation. In addition, all details and rules previously set out in delegated and implementing acts are included in the current legislative text (in form of Annexes) to ensure predictability. Most rules will therefore be known before 2021 to enable Member States start with implementation as early as possible.

Budget and content of Union funding

With regard to the allocation available for Germany, the figures contained in the proposal represent a cut of approximately 20% in resources. However, it is worth remembering that in 2014-2020, the allocation to Germany was protected by a safety net applicable to ex-convergence regions (i.e. changing their status from 2007-2013 to 2014-2020). This provision was worth more than EUR 5 billion for the Eastern Länder. This, together with the strong economic performance of the country (in terms of Gross Domestic Product and the labour market), explains the decrease in funding. The addition of an indicator on migration slightly offsets the decrease. Moreover, it should be noted that for 2014-2020 some of Germany's regions benefited from a one-off additional allocation worth ca. EUR 0.8 billion over and above what they would have been entitled to. Excluding this from the comparison, results in a more modest 17% drop in the allocation to Germany.

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

The Bundesrat voices objections as to the <u>use of both Gross National Income (at national level) and Gross Domestic Product (at regional level)</u> 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 and 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; also, Gross National Income data at regional level are not available systematically.

The Commission agrees that demographic trends, in particular those linked to the ageing of the working population, are extremely important to be taken into account. Nevertheless, this is an issue to be addressed rather through programming and not at the allocation of the available resources at EU level. The allocation formula takes account of available statistics at Union level. The Commission has carefully considered data availability for all regions and proposed to include a few new indicators that reflect in particular the development challenges that are necessary to be addressed.

<u>Regulatory framework and programming</u>

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

With regard to future small and medium-sized enterprises support, the Commission emphasizes that one of the big political priorities of the Union post-2020 is research and innovation (cf. the proposal to significantly increase the budget for Horizon Europe). 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 the policy objective 1 - "a smarter Europe by promoting innovative and smart economic transformation". While the codes for the types of intervention provide also for 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. The common output and result indicators also clearly reflect the focus on research and innovation. In any case, future small and medium-sized enterprises support 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.

Concerning the types of intervention, the proposal requires only an indicative breakdown of allocation by type of intervention. This is not a breakdown in budgetary terms (that is done at the level of a priority and reflected in the financial tables in the programme). However, different types of intervention reflect the commitments of the European Union budget to mainstream climate change actions and as such should be part of the Commission decision covering commitment appropriations for the cohesion policy. The types of intervention are set up to gather data in relation to planned expenditure that subsequently managing authorities are asked to report against. As in 2014-2020, they will feed the Open Data Platform[2]– a very successful tool appreciated by stakeholders and researchers. This information is of great value when reporting about cohesion policy to the European Parliament the Council.

Strategic approach and performance audit

On the performance framework, some clarifications are necessary in light of the change in the concept for the 2021-2027 period compared to the 2014-2020 period.

In 2014-2020, the performance framework is strictly connected with the 6% performance reserve. It results in additional funding for priorities that achieved their milestones during the performance review. It covers a subset of indicators at priority axis level (output or results indicators and financial indicators and when necessary key implementation steps). It does not encompass the result and output indicators (with targets) set up at each specific objective level – but they have to be set anyway for monitoring and evaluation purposes.

In 2021-2027, the performance framework is to allow for monitoring, evaluation, progress towards achievement of specific objectives and overall performance of the Funds – in line with the requirements of the Financial Regulation[3]. The performance framework covers all output and result indicators identified by managing authorities as relevant for their programme. It is important to note that for output indicators, milestones and targets are required. For result indicators, the proposal requires only targets (no milestones). In other words, the output and result form the programme's framework to assess its performance. But in general, compared to the 2014-2020 period, there are fewer types of indicators required (e.g. financial indicators and key implementation steps are not required).

The performance framework will not be linked to any performance reserve (the proposal for 2021-2027 did not retain the 6% performance reserve). Progress in achieving milestones for output indicators will be one of the elements taken into account during the mid-term review (next to new challenges resulting from the country-specific recommendations or changes in socio-economic situation). As such, it is an incentive for delivering results and channelling support to well-performing areas, however the assessment is not automatic; it is not linked to the achievement criteria as it was in the

2 *https://cohesiondata.ec.europa.eu/*
3 *Regulation (EU, Euratom) No 2018/1046*

2014-2020 period. The Commission together with the Member States needs to assess the performance of the specific objectives taking into account the objective or unexpected difficulties during implementation and potential remedy actions. These considerations will be taken into account when distributing 2026 and 2027 commitments to priorities.

Advantages of the new approach are: firstly, more transparency, clearer intervention logic, easier to understand by the outside world; secondly, more coherence – all data related to performance under the specific objective; and thirdly, a better link between the planned financial inputs and the expected output and results

The Commission's approach on enabling conditions is to enhance effectiveness of funding. In this regard, the objective is to ensure that supported operations are implemented within a favourable framework. The Commission notes the Bundesrat's request for clarification regarding enabling conditions. These create the necessary conditions to improve the effectiveness of implementation of the funds. The approach has been streamlined, with a reduced number of conditions and enhanced, more objective and tangible and clearer fulfilment criteria. The procedures linked to the enabling conditions have been simplified in terms of administration. However, their fulfilment needs to be respected throughout the period not only at the beginning; their follow-up is also reinforced. Member States will not be allowed to submit payment applications for the corresponding priorities if enabling conditions are not fulfilled, and this is not a mere recommendation but a clear-cut criterion. It will be a strong incentive to quickly remedy the missing elements for fulfilment. In this regard, it would be detrimental to the effectiveness of the Union's support if expenditure could be submitted and reimbursed prior to the fulfilment of the applicable conditions. In practical terms, it is however very unlikely that Member States could submit payment applications before the middle or even the end of 2022, given the necessary preliminary operational steps (adoption of programmes, setting-up of monitoring committees, launch of calls for projects and evaluation and selection of the bids). It will therefore leave sufficient time for Member States and regions to fulfil the conditions. It is noted that the detailed requirements at least on the sectoral elements mostly correspond to the measures which are undertaken by diligent authorities at programming stage.

The conditions do not address mechanisms to ensure compliance with the Union legislation. This falls under the competence of the Member States. However, they may aim at getting visibility for the contribution of the Union funding to support investments required for complying with the Union legislation, through preliminary needs assessment. Such assessments would anyhow be necessary for programming purposes.

With regard to State aid, the objective of the proposed enabling condition is to ensure that managing authorities have access to the updated information on undertakings in difficulties, to ensure compliance with the legal framework when granting European Union support. This suggestion stems from the experience of implementing the previous and current programming periods, where such risk has been revealed by audit. The Commission is nonetheless vigilant not to impose disproportionate burden in this regard.

The same approach will be applied on the proposed condition on public procurement. This latter aims at ensuring that the procurement systems are actually effective, by ensuring value for money through optimised competition in markets subject to procurement. The current situation is unfortunately not satisfactory, as the substantial share of single bids indicate. As a consequence, important over-costs are reported and the Commission believes it should be a shared concern of all Member States.

Concerning State aid, whereas European Union support granted under direct management is not considered subject to State aid, this is potentially not the case for the projects under shared management as they are implemented at the discretion of Member States. However, steps are being taken to simplify State aid treatment in this regard, for instance, by exempting from State aid rules the support to certain types of projects initially selected under the Seals of excellence mechanism of the Horizon programme. In addition, it is planned to revise the guidelines on regional aid, prior to the entry into force of the legislative package on cohesion policy.

On smart specialisation strategies, it is clear that these strategies are designed by regions, within collaborative processes (e.g.entrepreneurial discovery process). The Commission has therefore no intention to impose any revision of these strategies, and the proposed enabling conditions simply aim at ensuring that the existing strategies are implemented under sound governance mechanisms, guaranteeing their effectiveness and adaptability, and updated where necessary.

On enabling conditions, the Commission has proposed that they apply throughout the whole programming period, to ensure the effectiveness of funding. However, this requirement should not trigger administrative burden as the proposal does not require any monitoring system. Instead, the continuous fulfilment of the conditions is presumed and Member States should only inform the Commission if some major change may have an impact on the fulfilment.

Flexibility

As regards the Bundesrat's opinion on the flexibility elements of the Commission's legislative proposal, the Commission welcomes the Bundesrat's favourable opinion on the synergies between European Union policies. The Commission would like to underline that it will be up to the Member States to decide if they would like to transfer resources from the Funds to the centrally managed European Union policies. This opportunity is a natural consequence of the key guiding principle of an agile and flexible Union's budget for post-2020. Please note that, since such a transfer would require a programme amendment, the programme authorities and stakeholders will have to be fully involved in applying this option.

Regarding the non-substantial reprogramming, the Commission is convinced that the proposed limits are well-balanced, taking into account the responsibilities of the Commission for implementing the European Union budget as well as the differentiation of the programmes across the Union in terms of their volume.

The Commission takes note of the negative opinion of the Bundesrat as regards both the 5+2 programming and the mid-term review. The Commission is convinced that these mechanisms will introduce a budgetary flexibility, strengthen performance orientation of cohesion policy as well as the link with the European Semester. Abandoning the 5+2 programming will send a message that cohesion policy is a rigid policy that is not willing (or not able) to respond to emerging challenges nor to performance indicators. It will also make it difficult to take into account the country-specific recommendations during the mid-term review of the programmes.

The Commission also cannot share the argument that 5+2 programming would limit the possibilities to approve projects for a seven-year-long period. All long-term projects would need to be selected at the beginning of the period, as is the case currently. The need to ensure continuity of financing such projects will be taken into account during the mid-term review. For any projects selected and implemented after the review, there will still be four entire years for finalisation. In practice, it will work similarly as the performance reserve in the current programming period and there were no indications from the Member States or regions that this reserve prevented or slowed down implementation of long-term projects.

Interreg Europe and territorial instruments

The Commission takes note of the Bundesrat's concerns on the discontinuation of Interreg Europe. However, this is rather the result of a restructured and streamlined first Interreg component, not a genuine discontinuation. The Commission fully recognises the excellent work done by the Interreg Europe programme, supporting policy learning among public authorities to improve the performance of policies and programmes for regional development. To continue with the type of activities promoted by Interreg Europe, it is important to note that the Commission's proposal promotes and facilitates interregional co-operation activities within the national and regional programmes under the Investment for Jobs and Growth goal. It is also proposed that the existing INTERACT programme would be expanded to become a platform for policy learning and sharing experiences and best practices within the Interreg programmes, building further on the excellent work and achievements of Interreg Europe in the 2014-2020 and previous periods.

As regards territorial instruments (and in line with Annex I of the proposal, on the types of intervention - table 3 specifying codes for the territorial delivery mechanisms) Member States can choose between an integrated territorial investment (ITI), community-led local development (CLLD) or other – national – territorial tool focused on urban neighbourhoods, cities, towns or suburbs, or functional urban areas. Such other tools can literally be any other tools, already in place in various Member States, and different from integrated territorial investments. The Commission considers that there is a high degree of freedom in choosing such tools and there is no reason that only integrated territorial investments are used (which require pooling funding sources from more priorities of one or more programmes).

<u>*Technical assistance*</u>

The Commission proposal aims at simplifying the overall approach to reduce the administrative burden. Technical assistance would be implemented through a flat-rate financing based on progress in programme implementation, rather than through the reimbursement of technical assistance costs actually incurred and paid. By proposing to extend this simplified cost option to technical assistance, the Commission follows a key recommendation from the High Level Group for simplification. Also the European Court of Auditors encouraged the use of simplified cost options. Going back to real costs would complicate the system and discourage the use of the flat-rate.

The administrative costs associated with the European Regional Development Fund and the Cohesion Fund in 2014-2020 were below 3% of the average programme costs for the European Regional Development Fund and the Cohesion Fund as estimated in a recent study[4]*. The study also highlighted that greater use of simplified cost options (or financing not linked to costs) and a more proportionate approach to control and audits for the European Regional Development Fund and the Cohesion Fund could substantially reduce total administrative costs. The share of technical assistance in the total allocation for cohesion policy in 2014-2020 is around 3.2% of cohesion policy funds (Cohesion Fund, European Regional Development Fund and European Social Fund) programmed under shared management. In relation to Interreg programmes, due to the involvement of more than one Member State and the resulting higher administrative costs (in particular, in respect of controls and translation), the ceiling for technical assistance expenditure was proposed at a higher level than under the Investment for jobs and growth goal.*

In relation to the front-loading of technical assistance, first of all, technical assistance available in the 2014-2020 period can finance programme preparation. Furthermore, analysis of implementation data reported by Member States does not indicate the additional need for pre-financing specific for technical assistance.

Expenditure spent on technical assistance amounted, against overall spending for 2014-2020, for:

- *0.16% at the end of 2016 – to be compared with 1.5% of advance paid by end of 2023;*
- *0.46% at the end of 2017 - to be compared with 2% of advance paid by end of 2024.*

Based on the above figures, advance payments would be largely sufficient to cover all technical assistance expenditure incurred by the end of 2023 or even 2024, even in the (unlikely) absence of interim payments.

[4] *New assessment of administrative costs and burden in ESI Funds, Spatial Foresight & t33, https://ec.europa.eu/regional_policy/en/information/publications/studies/2018/new-assessment-of-esif-administrative-costs-and-burden*

Monitoring, evaluation, communication and visibility

The proposal requires reporting quantitative data six times a year, so that cohesion policy can present up-to-date data to the stakeholders. This would also enable effective communication on the achievements of the policy and would increase its political visibility. The reporting requirements relate to the managing authority – there is no obligation to impose on beneficiaries to report every two months.

Regarding performance, monitoring and data, the Commission aims at better monitoring the progress in implementation of the 2021-2027 programmes and thereby of the policy's contribution to the wider European Union objectives. This will be ensured by 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 be fed into the Open Data Platform in order to share the data with the wider public. Moreover, the approach to indicators across all policies will be harmonised – common result indicators can be aggregated and tracked for the Union as a whole. For all output and result indicators used in a given programme, a performance framework of milestones and targets will be established. The data transmitted by the managing authorities to the Commission and presented to the wider public will allow for assessment of the progress towards the milestones and targets. The annual implementation reports and progress reports used in 2014-2020 will be replaced by more flexible data and information transmission, which will significantly decrease administrative burden.

The Commission believes that visibility of the European Union's support is crucial to ensure its recognition by the general public. Therefore, citizens need to be informed of the use and benefits of the Union's support. Beneficiaries also have the responsibility to inform the public in that regard. On the other hand, the Commission agrees that this is to be done without creating unnecessary administrative burden. The aim of the provision is to avoid a duplication of visibility efforts and to make communication material available at all levels once supported through European Union funds. The Commission intends to make sure that copyright issues do not hamper the use of visibility material when paid for from Union resources.

As regards the financial correction possibility, the intention is to address a recurrent problem where beneficiaries (and some Member States) do not take visibility requirements seriously enough, and thus the general public is not informed of the presence and the added value of the European Union's support. Therefore, the possibility to sanction such behaviour was proposed to be introduced. This would not lead to additional audit burden, given that audit will - as in the past - need to ensure that all applicable law was complied with, and this includes (as in the past) rules concerning visibility requirements as well. The proposed rules do not imply additional requirements in relation to support through financial instruments, they merely clarify existing ones. Furthermore, the requirement for an A3 size display is not new, it existed in the past. Natural persons are usually not beneficiaries of such support and thus would not need to comply with this requirement. As regards the period during which such displays should be visible, it depends on the nature of the operations; therefore - as in the past - it would not be appropriate to regulate this at the European Union level.

Financial instruments

As acknowledged and appreciated by the Bundesrat, financial instruments are not promoted through binding targets. Rather, the Commission tries to promote their deployment through simplification and a more user-friendly framework. Building on the 2014-2020 rules, the Commission is now proposing simpler rules for the implementation of financial instruments, eliminating red tape and giving national authorities the necessary flexibility to implement financial instruments: This applies to many different fields, from ex ante assessment and payments to combination rules, amongst others.

By providing simpler and integrated rules and taking into account the principles of sound financial management, bodies implementing financial instruments (e.g. fund managers, financial intermediaries) will also be allowed to provide investment grants as well as grants to support the preparation of investments in addition to repayable financial products such as loans, equity and guarantees. This means that financial instruments and grants will be combined in one operation following the rules of a financial instrument operation instead of following two different sets of rules (applicable to financial instruments and grants). This type of grants can be in certain cases the unlocking factor for an investment to be implemented on the ground.

The reporting requirements for financial instruments have been aligned with those of grants – there will be no more separate reporting needed for financial instruments. If financial intermediaries are occasionally confronted with reporting or communication requirements that are more stringent than under their other activities, this is because scarce public resources are used to make cohesion policy's financial instruments attractive and supportive to final recipients, and this leads to higher transparency and accountability requirements.

The eligibility rules have been clarified, and rules on management costs and fees have been simplified while keeping them performance-based to encourage efficient management. For several years, the European Parliament as well as the European Court of Auditors have strongly criticised the very high level of management costs and fees for financial instruments supported by cohesion policy, compared to other Union level or private financial instruments. Therefore, the Commission proposed a solution which limits the level of management costs and fees and encourages the open selection of the bodies implementing financial instruments.

With regard to the Bundesrat's audit-related suggestions, based on Article 127 of the Financial Regulation, it is already possible to take into account the results of other independent audit work. The national audit authorities have to express their audit opinion in line with this Regulation and can use all the elements they consider appropriate in this respect.

On the notion of "undertakings in difficulty" 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 regulations of the 2014-2020 period. 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 start-ups are not excluded from receiving support, even if by their very nature they may 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.*

<u>Eligibility</u>

The proposed eligibility of value added tax for operations below EUR 5 million responds to simplification objectives. The experience of current and previous programming periods has indeed pointed out that national rules on recoverability of value added tax have sometimes led to complex legal issues, errors and subsequent financial corrections and thus to the legal uncertainty around value added tax eligibility. The current proposal provides legal certainty to beneficiaries and programme authorities. The proposed provision nonetheless does not prevent Member States from taking a more restrictive approach by not declaring or not making eligible value added tax at all.

Larger projects mostly correspond to infrastructure, implemented by public authorities for which the value added tax is often recoverable and therefore not eligible under the 2014-2020 rules. This also concerns a limited number of projects and beneficiaries (only 6% of the projects in terms of the number of projects). For these reasons the eligibility of value added tax has been limited to the proposed threshold.

With respect to touristic infrastructure, categories of expenditure 128 and 130, detailed in Annex I of the proposed Common Provisions Regulation, cover such investments. The category 15, related to "Small and medium-sized enterprises business development and internationalisation" covers, inter alia, business development activities of small and medium-sized enterprises active in the touristic sector, but not infrastructures.

Concerning the proposed compulsory use of simplified cost options, the purpose is to steer an effective take-up of such option, which has been very uneven under the current programming period. This option will trigger sharp simplification and reduction of administrative burden for managing authorities and for beneficiaries. This simplification will nonetheless only be effective as regards the declaration of expenditure by the beneficiary to the managing authority, as other applicable rules, such as on State aid or procurement will naturally continue to regulate the implementation of concerned operations. In this respect, the Commission does not see any argument for limiting the proposed scope of application of simplified cost options.

<u>Management, control, accounting</u>

In terms of management, control and accounting provisions for post-2020, the Commission explored all simplification avenues in view of reducing red-tape, complexity and control burden for all beneficiaries of cohesion policy. It looked into strengthening *the single audit principle and took account of lessons learned from the 2007-2013 and 2014-2020 periods, various recommendations from the European Court of Auditors in particular, as well as conclusions and recommendations of the High Level Group on simplification.*

The Commission appreciates the Bundesrat's support for abolishing designation procedures for the programmes post-2020 and for introducing a differentiated approach for audits of operations (Articles 77 to 79 of the proposed Common Provisions Regulation).

The proposal for the Common Provisions Regulation of 29 May 2018 has indeed, amongst others, the following aims: (i) to decrease the cost of controls and burden on beneficiaries and programme authorities while reducing complexities and ensuring radical simplification in all areas; (ii) to speed up programme implementation and ensure smooth transition between periods, building on the current system without fundamentally reconsidering the design and mechanism for cohesion policy funds, and (iii) to maintain the current assurance model allowing for an annual level of errors below 2% for each programme to ensure stability in the management and control systems established up to now.

The Commission also retained the notion of annual clearance of accounts and would like to reassure the Bundesrat that, for the period 2021-2027, the procedure will become even more robust (see Article 92(4) of the proposed Common Provisions Regulation).

Finally, in terms of management and control, please note that the European Court of Auditors' materiality level for irregularities and errors is set at 2% for the entire European Union budget. In order to align with this level, a higher percentage rate for irregularities was not considered.

<u>Country-specific recommendations</u>

Regarding the Bundesrat's rejection of <u>macroeconomic conditionality</u> in general, the Commission would like to refer to its reasoning provided under the heading of "Implementation", where it emphasized how important sound fiscal and economic policies are as a condition for sustainable economic growth and jobs and, consequently, for the successful delivery of cohesion policy.

The Commission does not expect constant and frequent readjustment of programmes just because of country-specific recommendations. Rather, the links with the country-specific recommendations will be strengthened already during the programming phase: they will be taken into account in programming at least on two occasions, at the beginning of the programming and during the mid-term review. Not only will there be horizontal alignment between the Semester and cohesion policy, but the country-specific recommendations formulated in these years will – to the extent possible – have a particular focus on investment needs (rather than on purely regulatory aspects) so that they can actually be implemented through cohesion policy. This way, the link between the Semester's recommendations and the programmes becomes more operational, and uncertainty can be avoided.

To the extent possible and where these appear to be serious causes of concern, the European Semester will also take into account regional disparities and specific regional problems. The 2019 Country Reports will adequately reflect the importance of the regional element.

Implementation

The Commission takes note that the Bundesrat welcomes the abolishment of the performance reserve, but rejects the "measures linking effectiveness of Funds to sound economic governance" as set out by Art. 15 of the proposal for Common Provisions Regulation. There is, however, no direct link between the two, and the macroeconomic conditionality defined by Art. 15 is not meant to "replace" the performance reserve.

In general, sound fiscal and economic policies are an important condition for sustainable economic growth and jobs and, consequently, for the successful delivery of cohesion policy. Therefore, cohesion policy and economic governance need to be linked. The Commission proposal basically maintains measures to promote sound economic governance. Macroeconomic conditionality has acted as an important deterrent, but on the sanctioning side it has been used very prudently, and sanctions have never been applied in practice. That does not mean it is "toothless" though. All the necessary prerequisites were already there in the 2014-2020 period and will continue – and sanctions are now linked to commitments as well as payments. The Commission will continue to ensure adequate use of sanctions, but the best deterrent is the one which never needs to be used.

Financial management

As far as the issue of available budget is concerned, the Commission has presented a Multiannual Financial Framework for 2021-2027 that is both realistic and ambitious. This required taking into account a wide range of issues, including Brexit, the need to provide support for new priorities and the need to ensure support for our regions and cities. This implies that some adjustments were needed in the cohesion policy budget as well as in the allocation for Interreg. What has to be kept in mind is that cohesion policy is still the largest policy of the Union in terms of financial volume and continues to cover all regions.

The Commission also notes the Bundesrat's reservations with regard to the 70% co-financing rate for Interreg, but also with regard to the reduction of the proposed European Union co-financing more generally. Co-financing rates were raised in a time of economic crisis to ensure the continuity of investment in regions hit hard by the crisis. A decrease is now being proposed to reflect the improvement of budgetary conditions across the European Union. Member States are consolidating their financial situation. The decrease should also contribute to greater 'ownership' as beneficiaries' financial interest would increase and should maintain if not increase the overall volume of public investments in key sectors of European importance.

The Commission also takes note of the Bundesrat's concerns with regard to the reintroduction of the N+2 rule. The Commission is convinced that the N+2 rule is *necessary. The current decommitment rule of N+3, combined with the high level of pre-financing, has been damaging for cohesion policy. It has led to excessively slow programme implementation – at least in financial terms – which has been heavily criticised. Pre-financing levels result from the overall situation of the budget in 2021-2023 in terms of the forecast of payment appropriations, taking into account the 2014-2020 execution of programmes. The progressive return to the N+2 rule, together with more than 80 simplifications proposed, is feasible and necessary to speed up the delivery of the policy: the N+2 rule, coupled with simplification and lower levels of pre-financing, would certainly contribute to speeding up implementation, especially if it goes hand in hand with lighter and more strategic programming and reporting requirements. The Commission has made several proposals to accelerate programming and ensure continuity across periods including through provisions promoting the rollover of management and control systems.*

European Social Fund Plus (ESF+)

On support to social partners, the Commission is convinced that full of social partners involvement in all stages of the programme, from initial design through to ex-post evaluation, is the best way to ensure that lessons learned from experience are used to improve policy design and effectiveness in the future. Therefore, the partnership principle will remain an important point in the preparation and implementation of shared management funds. However, there is evidence that social partners have weak capacity, that there is weak bipartite social dialogue, and that there is insufficient involvement of social partners not only in the design and implementation, but also in the monitoring and evaluation of reforms, policy-making and Funds' implementation. That is why it is extremely important for the Commission to continue to support social partners and their capacity in line with the principles of the European Pillar of Social Rights. Strong social partners are key to good and shared implementation of Union policies and funds.

With regard to the monitoring of data and indicators, Article 15(5) makes explicit reference to the provisions of the General Data Protection Regulation (points (c) and (e) of Article 6(1) of Regulation (EU) 2016/679) in accordance with which the Member States shall enable the Managing Authorities to obtain data from registers or equivalent sources. Data required in point (1b) of Annex I do not have to be asked from the participants (anymore), even if they are not available in registers.

Funds covered by the Common Provisions Regulation

Climate tracking remains and environment tracking is added to reflect the Multiannual Financial Framework proposal in relation to environment and climate objectives. Reflecting the importance of climate change in line with the Union's commitments to implement the Paris Agreement and the UN Sustainable Development Goals, the Funds will contribute to mainstream climate actions and the achievement of the overall target of 25% of the European Union budget expenditure supporting climate change objectives. Climate tracking, set up in Article 4(3) of the Common Provisions Regulation proposal, is based on weightings linked to the types of interventions to be found in the Annex I –

these types of intervention are part of the programme. The proposal for the Common Provisions Regulation has the intention not to repeat the general principles enshrined directly in the Treaty such as sustainable development. Article 67 of the proposal strengthens the actual implementation of these principles through the criteria for selecting operations. Furthermore, in order to assist regions facing challenges due to de-carbonisation challenges, European Regional Development Fund support under the Investment for Jobs and Growth will be concentrated on the policy objective of a 'greener, low-carbon Europe by promoting clean and fair energy transition, green and blue investment, the circular economy, climate adaptation and risk prevention and management'. Thematic concertation and climate tracking helps anchor sustainable development already at programming level.

<u>Environment</u>

The Commission welcomes the Bundesrat's support regarding the reference to the national energy and climate plans and the proposed flexibility in the event of natural disasters.

As regards the policy objective of dedicating 30% of the European Regional Development Fund resources on climate objectives, set out in recital 14 of the proposed European Regional Development Fund and Cohesion Fund Regulation, attention will be paid during the negotiation on programming, so that the future programmes consistently contribute to this achievement. However, for flexibility purposes, such policy objective cannot be translated into binding legal requirements applicable to each individual Member State, whose situation and needs differ. From the experience of current programming and taking into account the weighting of expenditure detailed in the Annex I of the proposed Common Provisions Regulation, the Commission is nonetheless confident that this objective will be largely met.

The Commission also confirms that climate change adaptation measures are taken into account for climate objectives, in accordance with afferent categories of expenditure (35, 36 and 37) detailed in Annex I of the proposed Common Provisions Regulation.

The Commission also confirms, pursuant to Article 11 of the proposed Common Provisions Regulation, that enabling conditions are fulfilled when all corresponding criteria are cumulatively met. As regards disaster management risks, these documents are already drafted and available in Member States. It appears therefore incorrect to conclude that the afferent enabling condition would trigger an overregulation.

Finally, the flexibility introduced regarding the purchase of land for environmental protection, is clearly set out in the proposed primary legal framework, and there is therefore neither legal possibility nor intention of the Commission to further restrict this provision through any future delegated acts.