Introduction

The Scottish Government is pleased to respond to the European Commission’s consultation on the future of cohesion policy within the EU. The consultation is timely. With the publication of the Fourth Cohesion Report and the initial discussion at the Fourth Cohesion Forum, we now have considerable evidence for reflecting on the impact of cohesion policy to date and the key economic and social development challenges facing the EU for the future. With the EU Budget Review, we have an opportunity to consider the role of cohesion policy within a wider-ranging debate on the current value added and future direction of the EU budget as a whole.

In Scotland, we believe cohesion policy should be considered in two ways. Cohesion policy can be viewed as the set of instruments dedicated to achieving the regional equity goals of the EU, notably the Structural and Cohesion Funds. However, there is a wider view of cohesion policy, which sees the goals of reducing regional economic disparities in the EU as a principle that should underlie all EU – and indeed, Member State, national and regional – policies. The cross-cutting nature of cohesion is particularly important in policy areas such as agriculture, innovation and State Aids. For this reason, we believe that cohesion will be a central issue for debate in the Budget Review consultation as well.

In Scotland, we take both ways of viewing cohesion policy seriously. We have a long and successful record of using Structural Funds in Scotland and recognise the value that the funding can add to the economic development efforts of nations and regions, as well as its limits and drawbacks. At the same time, we understand the value of mainstreaming cohesion as a principle in a wider range of policies and have reflected this in our recently-published Government Economic Strategy, which sets regional equity as part of the Strategic Priorities for the Scottish Government. With our history of using Structural Funds and our commitment to an economic policy that addresses the different needs of all parts of our nation, we believe our experience and insights will contribute to the wider debate over cohesion policy. In that context, our response complements the parallel response of the UK Government, to which we have contributed and which we support.

In presenting our response, we judge that, at this time, it is not appropriate to comment on the detail of future cohesion policy. Rather, our response focuses on several key insights and principles that we believe should inform the purpose of policy. Accordingly, we have not formally structured our response around the individual questions in the consultation document, but around the wider issues which they raise. These issues are:

1. the importance of cohesion and equity as an objective of EU policy (broadly covering questions 1-1.3 in the EU consultation document);
2. the need for EU cohesion policy to demonstrate value added in achieving this objective (broadly covering questions 2-2.4 and 3.3);
3. the value of supporting cross-border and transnational co-operation in the EU (broadly contributing to questions 2.1 and 3.4);
4. the challenge of a more flexible and joined-up approach to all EU policy support of cohesion (broadly covering questions 3-3.3; and
5. the risk of disproportionate financial and audit burdens placed on programmes (broadly contributing to questions 3.1 and 3.2).
1. The importance of cohesion and equity as a policy objective

Since the Treaty of Rome, cohesion has been a key objective of the EU. The original Treaty’s commitment to economic and social cohesion – and the Reform Treaty’s addition of territorial cohesion – highlights the fundamental importance of equity to the continuing development of the EU, not least as the Union continues to address the opportunities and challenges of enlargement. Its importance will not diminish after 2013, but only increase in the context of a larger and more diverse Union.

We believe that this commitment to cohesion complements the priorities of increasing jobs and growth as well as sustainable development set by the Lisbon and Gothenburg Agendas and welcome the efforts in the 2007-13 Budget for cohesion policy – particularly Structural and Cohesion Funds – to support both agendas. EU economic growth should take place within a framework of reducing regional disparities and a sustainable approach to the stewardship of our environmental resources. This alignment between cohesion, Lisbon and Gothenburg should continue in future with a greater integration of the strategic priorities set at EU level for supporting economic and social growth and cohesion, particularly through the Integrated Guidelines for Jobs & Growth and the National Reform Programmes.

The pursuit of cohesion is, of course, not restricted to EU, or indeed, Member State policy. It is an objective that permeates the economic development activities of all levels within the EU. This makes it important that a balance is found between ensuring policies complement each other and action is taken at an appropriate level and providing nations and regions with the flexibility and resources for achieving this.

Scotland offers a good example of how this balance can be struck. Our Government Economic Strategy sets out clearly a commitment to addressing the continuing differences in income, participation and growth across Scotland that act as a drag on economic performance and potential. The Strategy commits the Scottish Government to more and better employment in Scotland’s cities, towns and rural areas and sets a target of narrowing the gap in labour market participation between Scotland’s best and worst performing regions by 2017. It is important that that this kind of challenge is matched by a commitment to a target against which the policy can be measured.

Within this objective, we recognise that some regions require particular assistance. As part of our commitment to regional equity in Scotland, special attention is given to ensuring that the most remote areas of Scotland can contribute to, and benefit from, economic growth. For example, the Highlands & Islands region experiences sustained development challenges arising from population sparsity, dispersed business base, peripherality and infrastructure deficiencies. For this reason, we are pleased at the importance placed on territorial cohesion in the Reform Treaty and the recognition that peripheral parts of the EU can face significant challenges, not least with the shift to the east in the EU's centre of gravity. This recognition should continue to inform the development of EU policy.

At the same time, the diversity of problems faced by different regions must be recognised together with the need to avoid “one-size-fits-all” policy solutions. Urban areas with concentrations of social deprivation and poverty require a different range of policy tools and approaches to the fragile communities within some depressed rural areas. It is essential that cohesion policy does not prescribe the nature of the challenges, but accepts that different regions across the EU will face different obstacles in contributing to the EU's Lisbon and Gothenburg objectives. Subsidiarity within a common framework of shared objectives should remain a defining principle of cohesion policy.
2. The need for EU cohesion policy to demonstrate value added

EU cohesion policy has made important contributions to the goal of cohesion within Scotland for several decades. Not only have Structural Funds contributed to employment and economic growth, but they have supported a number of legacy projects, reinforced our domestic commitment to cross-cutting policy themes (such as environmental sustainability and equal opportunities) and from the start, helped to support a holistic strategic approach to economic development. At the same time, there are increasing costs associated with the implementation of Structural Funds, particularly those associated with the financial and audit control burden, as discussed in more detail below.

It is not clear at this point whether EU cohesion policy will continue contributing to our goal of greater Scottish equity within a more cohesive EU after 2013. We do not believe that cohesion policy should be a permanent fixture for any nation or region within the EU, but that its value should be tested against its real contributions to domestic – and EU – equity objectives. These considerations will depend to a large extent on the scope of cohesion policy, level of any additional resources it could bring to the nation and region and the costs of administering any future allocations.

As with other parts of the EU, Scotland will be making similar assessments of the value of EU cohesion policy to our own equity goals as the shape of policy becomes clearer closer to 2013. For this reason, the Scottish Government believes that the key test for EU cohesion policy should be its ability to bring added value to the efforts of nations and regions in reducing economic and social disparities, whether that value can be measured in terms of policy design, implementation or any genuinely additional funding that it can bring to domestic policy. In particular, we believe that cohesion policy can demonstrate that added value where the following principles are applied.

First, it is important that cohesion policy does not duplicate efforts at other levels of government. Additionality is the key test, both in terms of the policy activities covered by EU cohesion policy as well as the availability of any real, net additional resources to the policies of nations and regions.

Second, value added will be better demonstrated where there is greater spatial targeting of cohesion policy. The Scottish Government believes that the policy should be concentrated on those parts of the EU that experience the most difficult, intractable economic development challenges, wherever the areas are located, but particularly in the poorer Member States. Consequently, consideration should be given to developing a more refined approach to identifying and targeting spatial areas in need of support.

Lastly, there is a case for greater thematic targeting of EU cohesion policy. EU cohesion policy will not have the resources to cover the full range of potential policy interventions needed to reduce social and economic disparities. While nations and regions should be given the flexibility for implementing the policy, we recognise the need for the funding to be focused. The Commission consultation paper suggests that demographic and climate change may be areas where such targeting could take place in future – they are certainly issues of importance to Scotland – but there is also scope with respect to inter-regional co-operation as well, as we set out in more detail below.
3. The value of supporting cross-border and transnational co-operation in the EU

Territorial co-operation is an increasingly important element of Cohesion Policy. There is a real appreciation of the value of such programmes and acknowledgment of the tangible and lasting outcomes of co-operative projects. We wish to see these programmes well funded and their eligibility continue to be EU-wide after 2013. There is a significant Scottish commitment to participating in transnational and cross-border cooperation programmes during the 2007-13 period and we would wish to see these develop further beyond 2013.

However, recognition has to be given to the different status attributed to these programmes for regions based in mainland Europe with land borders and those in more peripheral island areas. For Scotland, as for many other regions and Member States, it is important that cross-border cooperation is not emphasised at the expense of transnational objectives. For example, demographics and climate change could legitimately feature as key themes, as both are of wider import and lend themselves to collaborative initiatives to address issues and transfer knowledge (all essential principles of the co-operation programmes).

4. The challenge of a more flexible and joined-up approach to EU policy

Greater EU cohesion is not just dependent on Structural and Cohesion Funds support, but other key policy areas such as:

- **State Aids**: as the ability to regenerate the worst-performing areas in a Member State will depend on the flexibility of State Aids rules;
- **R&D**: as support for research and innovation is critical for less-developed regions if they are not to fall behind wider EU growth; and
- **agricultural policy**: as cohesion and rural development strongly overlap.

Some of these areas will be discussed as part of the Budget Review. However, if cohesion is to be a key goal of the EU, it should feature in all EU policies and not be confined to one budget heading. Our Government Economic Strategy recognises that development can be best achieved where nations and regions have the full range of macro- and micro-economic policy levers to achieve its goals.

Consequently, we believe that the EU needs to give greater consideration to a joined-up approach to its different funding streams, focusing on equity outcomes as a whole rather than the specific, often unintegrated goals of the individual funding streams. This is particularly true of Structural Funds and rural development funding, where the dividing line between the objectives of both types of funding can be artificial. This is evident from the regulations governing each funding, which acknowledge the need for setting clear (though in operational terms, potentially over-bureaucratic) demarcation of funding that should be working to a common purpose. Again, in making these policies fit for the EU for the period after 2013, a new, more flexible approach, focused on the outcomes of policy, should be given serious consideration.

In Scotland, we have addressed a similar challenge with our landmark approach to local government funding. In November 2007, the Scottish Government reached a Concordat with COSLA, the representative body of Scottish local authorities. The Concordat recognised the importance of enabling local authorities to act with greater flexibility when using the funding provided to them from central government while securing a strong commitment to an agreed set of global outcomes. It removed an inflexible ring-fencing approach to funding and focused the collective attention of the Scottish public sector on the outcomes – rather than the outputs – of policy.
This outcome-based approach has considerable merit at the EU as well as the Scottish level. We would welcome a more flexible approach in how EU funding is used to support common EU goals. It is an approach that applies at much in relation to the way the EU budget is divided into separate and too often silo-based funding streams – such as Structural and Cohesion Funds and agricultural and rural development support – as well as in the rules governing the use of each fund. For example, with respect to Structural and Cohesion Funds, we believe that a more flexible approach could be taken towards the application of so-called Lisbon earmarking, which has been over-restrictive in prescribing the types of Structural Funds spending that nations and regions should undertake in support of cohesion and Lisbon and Gothenburg objectives.

5. **The risk of disproportionate financial and audit burdens on programmes**

Finally, the Scottish Government supports the aim of increasing flexibility and subsidiarity in designing and delivering Structural Funds programmes after 2013. We support the notion of a robust financial control system but would have reservations if this were to be applied as in recent years. There has been a disproportionate emphasis by the Commission since 2005 on financial and procedural rather than strategic issues. In the context of limited resources, this carries a risk that programme managers will be driven by the need to meet audit requirements rather than the need to build programmes whose projects have a strategic impact and deliver benefits to the local economy.

We would particularly raise our strong concerns about the rising levels of uncoordinated and apparently inconsistent financial audits undertaken by Commission services and the European Court of Auditors (ECA). Over-auditing of projects by EU auditors and the development of competing recommendations by different audit officials have placed a severe strain on domestic administrative resources without producing clear and proportionate gain. This has been exacerbated where new standards have been developed during the course of a programming period and applied retrospectively by auditors.

An associated difficulty has been the unwillingness of EU auditors to accept the assurance given by domestic certificates provided by independent professional experts. Audit certificates and quantity surveyor certificates, accepted as giving the necessary assurance to international standards by domestic auditors, are rejected by EU auditors without adequate cause being shown. This causes needless waste of effort and unnecessarily calls into question the financial probity of sound projects.

To strengthen the financial control system, we would make several recommendations. First, we strongly recommend a focus on outcomes – a feature of our own approach to domestic public spending in the Concordat with local government. Second, we wish greater co-ordination of EU audit responsibilities and schedules by Commission audit services and the ECA. Third, the Commission and the ECA should more actively explore ways to streamline the audit burden and pursue proportionality through greater use of assurances from national system accreditations. Lastly, the Commission should ensure that the demands made by audit requirements balance the risk of financial error against the need to develop programmes that achieve successful strategic impact.